REPORT OF THE

ROYAL COMMISSION OF INQUIRY

INTO DISCOUNTING AND ALLOWANCES

IN THE FOOD INDUSTRY IN ONTARIO

SEPTEMBER, 1980

His Honour Judge W.W. Leach
Commissioner

Rodney Hull, Q.C.
Counsel

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Royal Commission of Inquiry into
Discounting and Allowances
in the Food Industry
in Ontario

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September, 1980.

To His Honour,

The Lieutenant - Governor of

The Province of Ontario

May It Please Your Honour:

On the 7th day of February, 1979, I was duly appointed to inquire into discounting and allowances in the food industry in Ontario.

I have carried out the duties as specified in the Order-In-Council, and submit herewith my Report.

Judge W.W. Leach,

Commissioner

Copy of an Order-In-Council approved by His Honour the Administrator of the Government of the Province of Ontario, dated the 23rd day of August, A.D. 1978.

Upon the recommendation of the Honourable the Minister of Agriculture and Food, the Committee of Council advise that the marketing of food and grocery food products, from producers or importers through to retail sale to the consumer in Ontario is an activity of importance and concern to the public of Ontario;

The Committee further advise that pursuant to the provisions of The Public Inquiries Act, 1971, Statutes of Ontario, 1971, Chapter 49, a commission be issued appointing

His Honour James Frederick William Ross

District Court Judge, Thunder Bay,

a Commissioner under the designation "Inquiry into Discounting and Allowances in the Food Industry in Ontario" to inquire into and make recommendations respecting,

(a) discounts, allowances, rebates or other forms of payment offered by or exacted from persons engaged in the marketing of food or grocery food products and paid or allowed directly or indirectly to purchasers thereof other than discounts, allowances, rebates or other forms of

payment paid or allowed directly to the consumer; and

(b) the effect, if any, of the practices referred to in clause (a) on price spreads or on the level of prices,

(i) paid for food or grocery food products by Ontario consumers, and

(ii) paid to the farmer in Ontario for agricultural food items produced in Ontario,

and to make such recommendations generally with respect thereto as, in the opinion of the Commissioner, would be applicable to Ontario and of benefit to the people of Ontario.

And the Committee further advise that for the purpose of this inquiry,

(a) "food" means meat, eggs, poultry, dairy products, grains, fruit, fruit products, vegetables, vegetable products, maple products or honey products produced for human consumption;

(b) "grocery food product" means a manufactured article for human consumption derived in whole or in part from food;

(c) "marketing" means marketing as defined in The Farm Products Marketing Act.

And the Committee further advise that all Government ministries, boards, commissions, agencies and committees shall assist the Commissioner to the fullest extent in order that he may carry out his duties and functions and that he shall have the authority to engage such counsel, research, and other staff and technical advisors as he considers proper.

Certified,

"R.A. FARRELL"
Deputy Clerk,
Executive Council

Copy of an Order-In-Council approved by Her Honour the Lieutenant Governor, dated the 7th day of February, A.D. 1979.

The Committee of Council have had under consideration the report of the Honourable the Minister of Agriculture and Food, wherein he states that,

WHEREAS Your Honour, by Order-In-Council numbered O.C.2537/78 dated the 23rd day of August, 1978, authorized the issuance of a commission appointing His Honour James Frederick William Ross, District Court Judge, Thunder Bay, a Commissioner under the designation "Inquiry into Discounting and Allowances in the Food Industry in Ontario" to inquire into and make recommendations respecting the matters therein set forth;

AND WHEREAS, the said Commissioner has found himself unable, through ill health, to continue;

The Honourable the Minister of Agriculture and Food therefore recommends that the said Order-In-Council be amended by striking out "His Honour James Frederick William Ross, District Court Judge, Thunder Bay" in the twelfth and thirteenth lines and inserting in lieu thereof,

> "His Honour Wilfred Wesley Leach, County Court Judge, Judicial District of Haldimand."

The Committee of Council concur in the recommendation of the Honourable Minister of Agriculture and Food and advise that the same be acted on.

Certified,

"R.A. FARRELL"

Deputy Clerk,

Executive Council

ISSUES

The Commission, by its terms of reference, is charged with a two-fold responsibility, namely, to inquire into and make recommendations respecting,

(a) discounts, allowances, rebates or other forms of payment offered by or exacted from persons engaged in the marketing of food or grocery food products. Rebates or other forms of payment made directly to the consumer are excluded.

(b) The effect of these, if any, on the price spread or on the level of prices,

(i) paid by the Ontario consumer, and

(ii) paid to the farmers of Ontario for agricultural food items produced in Ontario.

SUMMARY OF CONCLUSIONS

The following is a summary of the major conclusions of the Inquiry. All of the conclusions reached in individual chapters are collected in the final chapter of the Report.

1. The system of discounts, allowances and rebates is highly developed in the food industry in Ontario.

2. There is much confusion and misunderstanding among some farmers, some processors and some retailers concerning the operation of the rebate system.

3. It does not appear that the Ontario farmer or farm prices are adversely affected by the rebate system.

4. It appears that there is no significant difference in the level of rebates granted by small or large processor/manufacturers. In other words, the rebate system is not a resolution of market power that favours either large or small processor/-manufacturers.

5. It appears that there is no significant difference in the level of rebates received by small or large retailers. In other words, the rebate system is not a resolution of market power that favours either large or small retailers.

6. It does not appear that the Ontario consumer or consumer prices are adversely affected by the rebate system.

7. The conclusions of many reliable studies indicate that, based on his disposable income, the consumer in Ontario purchases quality foods at prices that are among the lowest in the world.

RECOMMENDATIONS

1. That no further inquiries be conducted into discounting practices in the food industry, unless persuasive and substantial evidence is adduced that such an inquiry is required. Inquiries add to the cost of food to the consumer and increase his tax bill.

2. That the sale of wine be permitted by both large and small retailers.

3. That the Legislature consider the establishment of a forum, outside government, to mediate problems between the various levels in the food industry, and to clear up the confusion about rebating practices. For details, see Chapter 18, Overview of the Food Industry.

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PREFACE

The Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario was established by Order-In-Council of the Ontario Government on the 23rd day of August, 1978. His Honour Judge James F.W. Ross, since deceased, was appointed sole Commissioner. On February 7, 1979, due to the ill health of Judge Ross, an amending Order-In-Council was passed appointing me sole Commissioner to complete the Inquiry. Rodney Hull, Q.C., was appointed as Commission Counsel by Judge Ross. Heather Werry was named Registrar.

Commissioner Ross, appreciating the complexity of the Inquiry, retained Laventhol and Horwath, Management Consultants, to assist the Commission with research, investigation and financial analysis. The consultants commenced their duties in November, 1978. The Commissioner, in consultation with Mr. Hull, set out the format the Inquiry would take.

Many difficult decisions had to be made. To answer the Terms of Reference with any degree of certainty, the Inquiry had to ascertain, in fact, the actual amount of discounts and allowances being paid by processor/manufacturers to retailers, wholesalers, and buying groups. These firms strongly objected to their individual figures on specific products being made public as they claimed it would impair their competitive position and would disrupt the food industry. They were not opposed to the public

knowing the actual figures but they were opposed to revealing trade secrets to their competitors.

To solve this dilemma, Commissioner Ross decided that questionnaires would be sent to a broad sampling of processor/manufacturers, retailers, wholesalers and buying groups, asking the firms to complete and return them (Appendices 4 and 5). The questionnaire asked for the specific figures relating to the various kinds of discounts, as well as for other information. The completed questionnaires were to be returned in confidence, to the Commission's consultants, who were sworn to secrecy. The Commission's consultants checked, collated and reported the results in an aggregate form to the Commission.

This procedure provided the Commission and the public with actual figures for discounting. At the same time, it protected the competitive position of any respondent firms. Upon continuing the Inquiry, I adopted this rational solution to a thorny problem.

Notices of the Preliminary Hearing to be held in December, 1978, were published in newspapers throughout the Province. In addition, 1,300 letters were sent by Commission Counsel to members of the food industry requesting submissions. Judge Ross conducted the Preliminary Hearing on December 7th. However, for health reasons alluded to earlier, he was unable to continue with the Inquiry.

I was appointed on February 7th to continue the Inquiry and I duly reconvened the Inquiry on February 14th.

Advertisements were again inserted in newspapers throughout Ontario and letters sent to various members of the food industry requesting input.

The Inquiry hearings resumed on February 14, 1979 and 50 days of hearings were held with the last day of hearings being held on October 25th, 1979. Counsel and parties represented at the hearings at this time were asked to file written submissions by December 3rd, 1979. The transcripts of evidence totalled 4,465 pages. Witnesses heard totalled 110 (Appendix 1), and 150 exhibits were filed (Appendix 2).

In writing this Report, I have considered the comprehensive research of the consultants, the oral evidence, briefs, background material and submissions of counsel for all persons represented at the hearings.

I hoped in writing this Report that I could present it in an attractive, readable style so that the public could be better informed about discounting in the food industry. I have fallen short of this objective for two reasons. First, the food industry is one of the most complex industries in our Province. Second, it possesses a jargon of its own with dialects at different levels in the food chain.

ACKNOWLEDGEMENTS

An inquiry cannot be conducted with any degree of success unless the Commission has an efficient and dedicated staff. I was fortunate in having such a group.

The Commission is indebted to Rodney Hull, Q.C., General Counsel, for his dedicated efforts in organizing the conduct of the Inquiry in all its aspects.

Mr. Hull was ably assisted by Robert Weist, Assistant Counsel and Registrar, who provided invaluable input to the Commission by researching many subjects requested by me to be investigated. Heather Werry was also a very efficient Registrar during her tenure with the Commission.

The work of Laventhol & Horwath, Management Consultants, was outstanding. I shall deal more specifically with their role in the course of the Report. Suffice it to say, the Inquiry could not have been conducted efficiently without their input. Their team consisted of:

Ralph Fisher, F.C.A., C.M.C.
Project Director
David F. Ross, M.B.A.
Research Staff
Howard Mednick, M.B.A., M.A.
Research Staff
Jeffrey Kantor, C.A.
Research Assistant

I appreciate their co-operation and patience in explaining to me the many complex financial analyses they carried out. I am particularly grateful to David Ross, who became Research Consultant to this Commission, for his comprehensive research and co-operation.

I am grateful to my secretary, Mrs. Betty MacDonald, for her efforts in arranging my judicial duties during my absence at the Inquiry hearings, and for typing the draft of this report. The Commission had several secretaries, and they were all most helpful. I particularly want to thank Ms. Gwen King, Mrs. Jan Gordon and Mrs. Carroll Brooks for their efforts in typing and re-typing the Report.

The Commission received excellent co-operation from the many producers, wholesalers, processors, manufacturers, retailers and trade and farm associations. All government ministries, boards and agencies assisted, when requested. I am appreciative of the assistance of Mr. Peter Clendinneng and Mr. Roland D'Abadie of the Ministry of the Attorney General for their guidance concerning the Commission budget. The Ministry of Agriculture and Food, as well, co-operated fully with the Commission, when asked, in providing statistics and other information.

Many counsel appeared on the Inquiry, and without exception, conducted themselves in a highly ethical and co-operative manner. I am indebted to those persons who replied to the questionnaires and submitted briefs. The

briefs were all well prepared and presented and were invaluable in preparing my Report.

And last, but certainly not least, I thank my wife who tolerated me during the hearings and the writing of this Report. At times, she expressed the consumers' view quite forcefully!

CHAPTER 1

INTRODUCTION

INTRODUCTION

BACKGROUND OF INQUIRY

In the spring of 1978, the Minister of Agriculture and Food presented his estimates to the Legislative Assembly. A debate ensued in the Legislature, during which the opposition parties questioned the Minister about the practice of discounting in the food industry. The allegations were focused on discounts pertaining to milk and fresh vegetables.

This debate indicated there was much suspicion, fear and confusion within the industry and in the public's mind about discounting practices.

The problem was referred to the Resources Development Committee which conducted an inquiry before which witnesses were called. The Committee recommended in its report that a royal commission be appointed. This report motivated the constitution of this Inquiry.

The Minister of Agriculture and Food opposed such an inquiry as he was of the opinion that it was not needed. He expressed the view that the Inquiry would be one of the longest and most expensive in the history of the Province, but I am pleased to report that this was not the case.

TERMS OF REFERENCE

The Terms of Reference can be stated briefly as follows:

The Commission was charged to inquire into and make recommendations concerning:

(a) discounts, allowances and rebates in the food industry;

(b) the effect of these on prices paid to the farmer for agricultural food items; and,

(c) the effect of these on price spreads or the level of prices to the consumer.

This was not an inquiry into food prices. I am afraid, however, that the public felt that this was its purpose.

SCHEME OF REPORT

The food industry is very complex and not fully understood by the consumer, and, in many cases, not fully understood by persons engaged in it. For this reason, I felt it necessary to describe in detail the various links in the food chain -- farmer, importer, processor/-manufacturer, buying group, wholesaler, large and small retailer and consumer. Rebates are considered at each level. This has resulted in some repetition, but hopefully will clarify the workings of the industry to the reader.

In addition, other chapters and sections of chapters are included in the Report which relate directly or indirectly to the terms of reference. These include: Catalogue of Rebates, Cost Justification of Rebates, Concentration in the Industry, Loss Leaders, Listing and Delisting, and Rebates and the Law. Other chapters are: Findings of Other Inquiries and an Overview of the Food Industry.

At the end of each chapter I have summarized my conclusions relating to that segment. These conclusions are aggregated with my recommendations in the final chapter.

QUESTIONS TO BE ANSWERED

1. WHAT ARE DISCOUNTS, ALLOWANCES AND REBATES IN THE FOOD INDUSTRY?

Discounting terminology is confusing to people outside the industry. Generally speaking, discounting practices involve payments that flow from food processors to the food retailers. There are many different types, and these are listed and explained in Chapter 2. Throughout my Report, the term "rebate" has been used as a generic term for all forms of discounts, allowances and rebates for the reason that this term is the most general of the three terms and the most generally used in the food industry. The terms "discounting" and "rebating" are used interchangeably throughout.

2. HOW DOES THE REBATE SYSTEM AFFECT ONTARIO FARMERS?

See Chapter 3.

3. IS THE REBATE SYSTEM A RESOLUTION OF MARKET POWER?

A concern in the public mind is that whoever wields the greatest power receives the most favourable discounts. This theory could apply in two ways. The first application is that large processors may be able to resist pressure to grant discounts more successfully than small processors.* The second application is that small retailers may be unable to exact as fair a rebate as large retailers. Chapters 5, 9, and 10 will review both of these theories in light of the evidence received.

4. ARE REBATES PASSED THROUGH TO THE CONSUMER?

This is the area of most interest to the public. I will deal with this issue in Chapter 9.

5. ARE LARGE RETAILERS ABLE TO CONTROL PRODUCTS SOLD BY REBATES?

This question is dealt with in Chapter 15.

*"Processor" means original manufacturer of a food product. The terms "processor" and "manufacturer" will be used interchangeably in my Report.

CONDUCT OF THE INQUIRY

The Inquiry had two major aspects:

(a) public hearings, and

(b) investigation and research by Inquiry staff and consultants.

The hearings were conducted at 180 Dundas Street West, Toronto, and were open to the public and news media. Any person who had an interest in the Inquiry was entitled to be represented by counsel or to appear personally at the hearings.

Most witnesses presented a brief, copies of which were filed with the Commission and were distributed to counsel, news media and other interested parties. Mr. Hull examined the witnesses to elicit the evidence required to answer the terms of reference. Counsel, or other persons present, were then given the opportunity to cross-examine and re-examine the witnesses. Counsel, in most cases, were most co-operative in following my request not to duplicate the questioning. The evidence given at the hearings was recorded and transcribed.

CONSULTANTS' ROLE

As previously stated, this Inquiry could not have been conducted with any degree of efficiency without the input of the consultants, Laventhol & Horwath.

The consultants conducted a questionnaire survey of processors, wholesalers, buying groups and retailers to

ascertain the facts necessary to properly respond to the terms of reference. The processor/manufacturer questionnaire (Appendix 4) was sent to 123 firms. These firms represent a large proportion of that segment of the industry. The retailer questionnaire (Appendix 5) was sent to 25 firms. Included in the list were all major food chains in the Province as well as several prominent minor chains. The consultants also carried out a survey of ten small non-chain independents. Wholesalers and buying groups were also thoroughly surveyed.

The completed questionnaires were analyzed by the consultants and followed up with interviews to clarify any apparent discrepancies. In addition, the consultants attended at the hearings to ascertain that the oral evidence was in accord with the replies. They carried out extensive research and interviews of all sectors of the industry. From time to time during the Inquiry, I called upon the consultants to research certain issues raised at the hearings.

Upon completion of their survey, the consultants provided me with a comprehensive study of their findings. I have used many parts of this study in my Report as it reflects accurately the actual picture of discounting in the food industry.

After reading other reports of inquiries into the food industry in Canada, I have concluded that the consultants' research was the most extensive and thorough that has been conducted to date.

BASIS FOR REPORT

My report is based on:

(a) evidence from the hearings including exhibits, briefs and oral testimony;

(b) the consultants' report; and,

(c) investigations conducted by myself and Inquiry staff.

CHAPTER 2

THE ONTARIO FOOD CHAIN

GENERAL

Food is vital to our lives. As we partake of a meal, our main concerns are flavour, quality and quantity; the emphasis varies with the individual.

Prior to consumption, the average consumer's acquaintance with food is when he purchases it from the retailers' shelves. He has little knowledge, and understandably so, of how it reaches the shelf.

The food industry operates daily in the midst of public awareness as to prices and quality at the retailer level. In these days of inflation, public awareness is particularly heightened. This public concern is not applicable, to such a degree, to other industries that serve our material needs.

Several witnesses testified that the food industry is one of the most complex in our province. I heartily agree. Before turning to the main focus of this Inquiry, it is essential to have a basic understanding of the various levels in the various food distribution systems. Figure 2-A is a simple graphic portrayal of the food chain from producer to consumer.

In the first instance, all food, other than synthetic food, is produced by a farmer. In most cases, food

consumed in Ontario is grown by an Ontario farmer. Because we reside in a northern climate with a short growing season, we must import certain foods from other countries. For example, the farmers of California, Arizona and Florida produce many of the fruits and vegetables consumed in Ontario in the winter months. This subject is dealt with more fully in Chapter 4, Imports and Rebates.

Between the farmer and the consumer is a variety of organizations whose actions and decisions affect the producer. The colloquial expression for these organizations is "the middlemen." Figure 2-A illustrates some of these institutions. In fact, the figure is too simplistic because it does not depict the important role which transportation companies, financial institutions and advertising agencies play in the food distribution system.

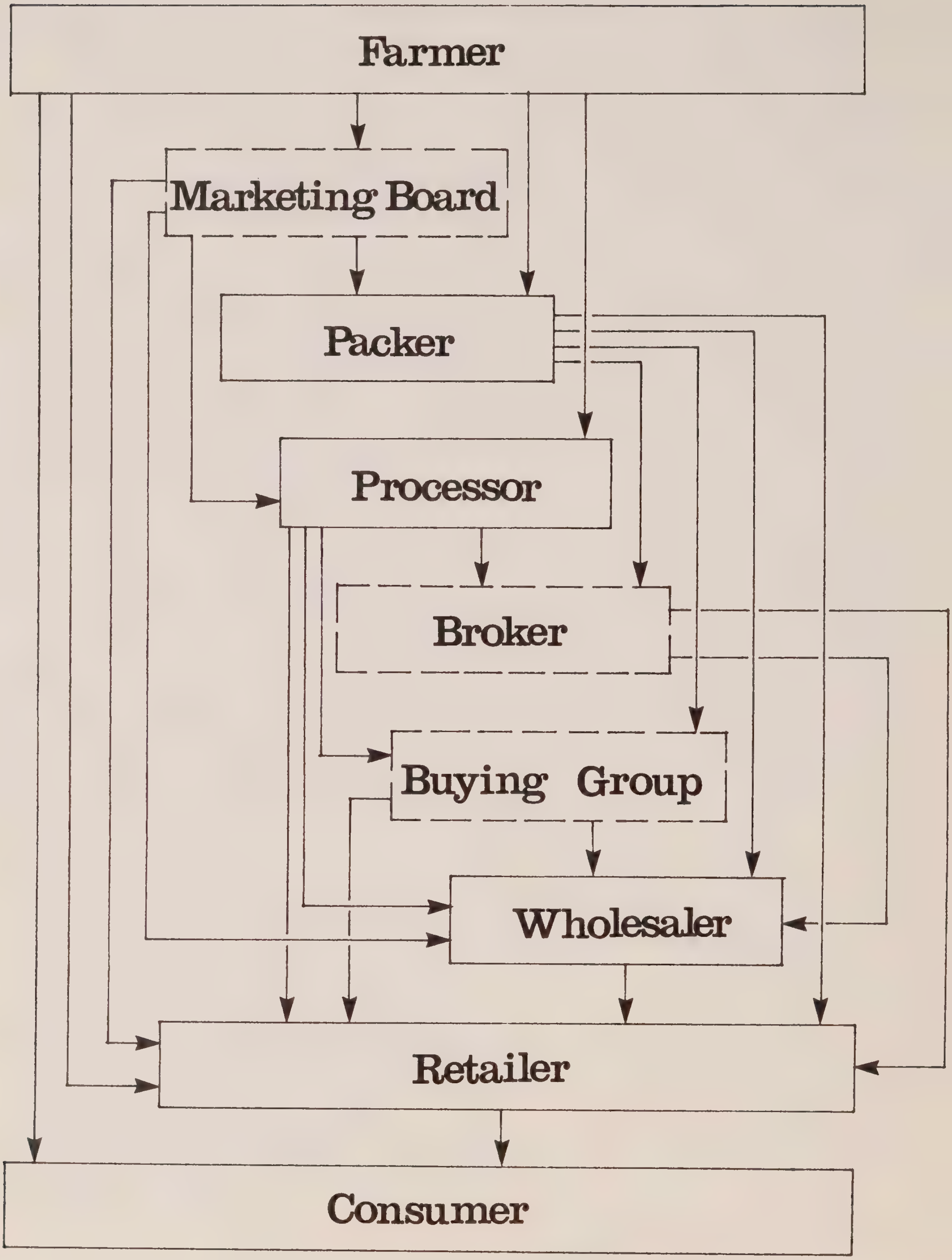
I shall now deal briefly and generally with the main components in the food chain. Specific figures and sources will be presented and discussed in the chapters devoted to each link in the food chain.

THE FARMER

Ontario farmers produce a wide variety of food products of excellent quality. In 1978, Ontario farm cash receipts for the various products amounted to more than $3 billion. This subject is dealt with in detail in Chapter 3, Effect of Rebates on Farmers.

FIGURE 2-A

THE ONTARIO FOOD CHAIN



NOTE: Broken line box indicates that the organization generally does not take delivery of product.

The Ontario farmer markets his produce in a variety of ways. The majority of Ontario farm cash receipts are from products which are sold pursuant to Ontario marketing board regulation.

The remainder of Ontario farm cash receipts comes from products which are not under marketing board jurisdiction. Farmers sell their products in a variety of ways -- at roadside stands, at the Ontario Food Terminal, to packer-shippers, to processors, to retailers, directly or through brokers.

In 1978, Ontario imported agricultural products worth just less than $2 billion. This represents an amount equal to over one-half of the value of Ontario farm cash receipts. Ontario accounts for about 40% of all Canadian agricultural imports.

Imported farm products may also pass through a variety of middlemen before arriving on the retailer's shelf. The Ontario buyer either contacts the out-of-province producer directly or his local agent, and arranges for the produce to be imported across provincial boundaries. For further information, see Chapter 4, Imports and Rebates.

THE PACKER

The packer buys fresh produce from the farmer, prepares it for market, and then sells it to wholesalers or retailers, either in or out of the province.

In the fruit and vegetable area, certain growers also pack for themselves and other growers. These firms are called grower/packers.

THE PROCESSOR/MANUFACTURER

A food processor or manufacturer purchases farm products from the farmer or farm marketing organization. He transforms this original product into various food products and sells to wholesalers or retailers.

The function of the manufacturer/processor varies with the food commodity. For example, a meat processor purchases livestock and dresses it for sale as fresh meat or processes it for sale as cured or canned meat. Flour and cereal product manufacturers mill wheat and other cereal grains into flour and cereals. The fluid milk processor, commonly known as a "dairy", purchases raw milk from the Ontario Milk Marketing Board and processes it for many dairy products.

These are just a few illustrations taken from the multitude of food processors and manufacturers.

THE BROKER

A food broker deals in the sale of food and related products for food producers, usually within a specific geographical area.

Many food producers, mainly manufacturers and processors, retain food brokers to arrange the sale of their products to the wholesale and chain retail buyers. This is an advantage to the producer who does not have to retain a permanent sales force to serve a market.

Food brokers generally handle most products sold in grocery outlets except certain perishable products such as eggs and milk.

The importance of the food broker in the food chain is indicated by the fact that food products sold by Ontario food brokers may amount to as much as 43% of the total food sales in Ontario.*

The function of the food broker varies and depends on the contract with his principal. Food brokers are usually paid on a commission basis.

THE BUYING GROUP

The buying group is a group of wholesalers or retailers who join together to purchase food products.

The buying group, though owned and controlled by its member shareholders, is generally an incorporated legal entity separate from them. One major exception is the buying group known as Intersave which is a division of Loblaw Companies Limited.

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* As estimated by the Ontario Food Brokers Association in its sales survey, January 14, 1980, undertaken at the request of the Commission.

The main advantage of joining a buying group is that buying groups can obtain higher levels of volume rebates on purchases than shareholding members could obtain buying individually.

The buying group does not deal with all levels of the food chain but only with those suppliers that offer volume rebates and private label products. Buying groups carry out a variety of functions for their members. These functions and the impact of buying groups are developed more fully in Chapter 7, Buying Groups and Rebates.

THE WHOLESALER

A wholesaler purchases a product in large quantities, warehouses it, and then resells it to a retail outlet on demand. This description is applicable to both grocery wholesalers and fruit and vegetable wholesalers.

Major grocery wholesalers, such as National Grocers Company Limited, M. Loeb Limited, Oshawa Group Limited or Lumsden Brothers Limited, generally have two types of selling operations:

(a) The traditional type, in which the retailer orders his goods by phone or telex and the wholesaler loads and transports the goods by truck to his customer.

(b) A more recent type of operation is called "cash and carry". The retailer or his

agent attends at the warehouse, selects his goods, pays cash and transports the goods to his store.

The fruit and vegetable wholesaler purchases directly or through a broker from Ontario packers and growers and from American and other foreign produce firms. In most cases, these wholesalers distribute from refrigerated warehouses to every type of retailer from independents to the large chains.

THE RETAILER

The food retailer sells to the consumer who is the last link in the food chain. Ontario has a wide variety of food retailers ranging from large chains to "ma-pa" stores.

The retailer purchases from every level of the food chain.

In order to answer the terms of reference it was necessary to focus on the "chain store organizations." Statistics Canada defines this term as any organization operating four or more retail outlets, and I have adopted this definition for my Report.

In Ontario, this definition includes the large chains such as Dominion Stores, Loblaws, Steinberg's and A & P with many outlets and smaller chains such as Knob Hill Farms with five outlets. The definition also includes the

chains of so-called "convenience stores" such as Becker's or Mac's Milk.

Any firm not meeting the definition of chain store organization is automatically classified by Statistics Canada as an "independent" and such terminology is adhered to in this report.

The distinction between chains and independents will be more fully considered in Chapter 13, Concentration and Rebates.

ORIGIN AND RATIONALE FOR REBATES AND ALLOWANCES

Since merchandising began in the free enterprise system, buyers and sellers have negotiated special arrangements. This is based on the natural desire of a buyer to purchase as cheaply as he can and that of a seller to realize as high a price as he can. For example, a buyer usually expects a cash discount if he pays within a specified time. He also looks for a volume discount if he purchases a certain quantity. Today, with the growing complexity of all industry, discounting practices have also grown more complex and confusing.

The food chain has several links engaged in discounting -- the producer, processor, wholesaler and retailer. Discounting affects profits and since everyone is in business to make a profit, discounting is of importance to the whole food chain.

Farmers and importers are the sources of raw food. Generally, rebates are not significant at this level. See Chapter 3 for the effect of rebates on farmers.

Rebates are paid almost exclusively by sellers of manufactured products. The distinction between processing and manufacturing is not important for this Report as both processors and manufacturers use rebates in the same way.

Rebates are received by retailers, wholesalers, buying groups, consumers and occasionally, by other manufacturers. Rebates, in some cases, are paid to the consumer directly in the form of coupons. Such direct payments are expressly outside the terms of reference of this Inquiry. In any event, the bulk of rebates move through the chain to the consumer, as explained in Chapter 9.

In order to get their products on the retailers' shelves, processors have developed a system of rebates and allowances paid to the wholesaler or retail chain. These are considered "incentives" for good shelf space and reduced prices to the consumer.

The retail level of the food chain depends on high volume of sales and frequent rotation of stock. Retailers used the word "velocity" on many occasions throughout the Inquiry to describe the basis for success in their operations.

Most witnesses for the retail chains described rebates as "earned cost reductions." They submitted that on volume

discounts, they "earned" the rebate because a manufacturer who can produce and ship in quantity is realizing a reduction in cost which should be passed through to the consumer. Large volumes maximize the productivity of the manufacturer's plants and facilitate financing.

Retailers also submitted that they earned the advertising and service rebates. Upon the creation of a new product, manufacturers grant introductory allowances. The rationale for this allowance is that the manufacturer should pay for a new product's introduction as shelf space is limited and the retailer has to remove a profit-making product to make room for it. Larger manufacturers can stimulate consumer demand by national advertising. Smaller manufacturers cannot afford such advertising and often buy advertising in the wholesalers' or retailers' advertising programs.

The wholesale and retail levels of the industry make day-to-day management decisions as to the products to be listed or delisted. See Chapter 14, Listing and Delisting.

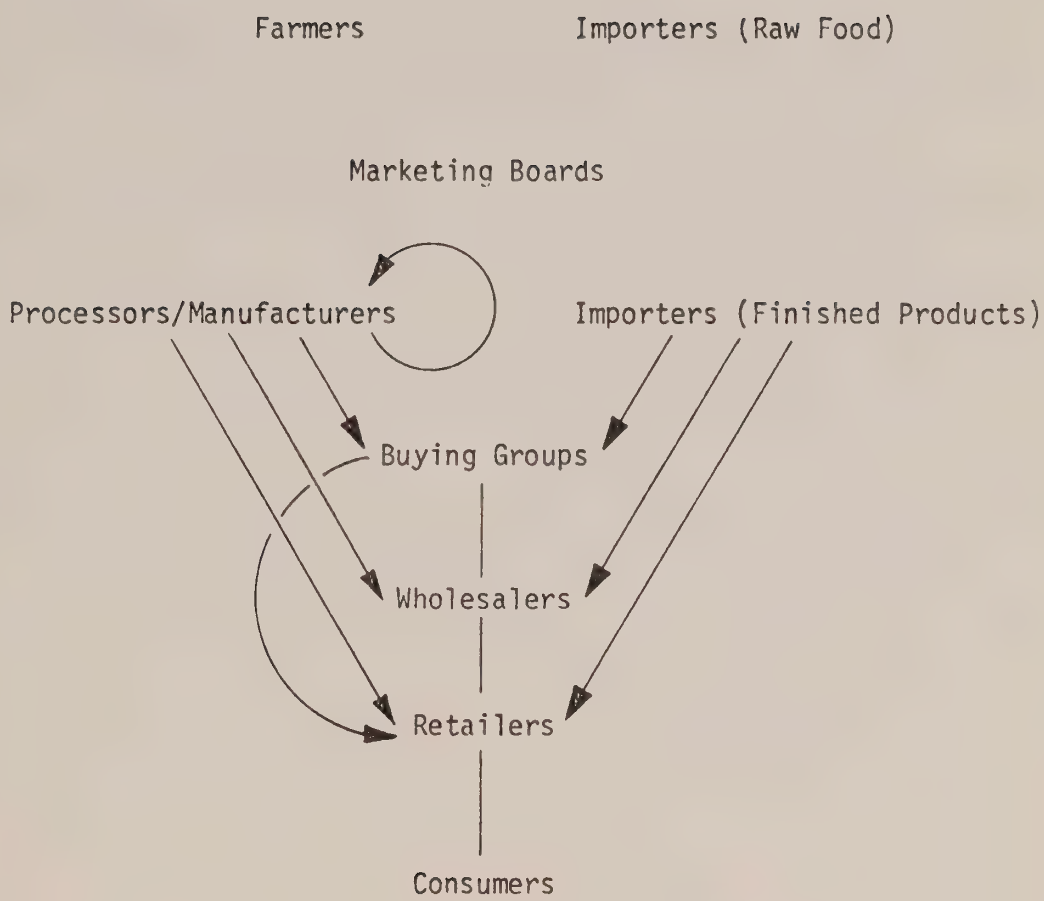
TERMINOLOGY - CATALOGUE OF REBATES

REBATE FLOWS

Figure 2-B is a simplified view of the rebate flow through the food chain. The figure indicates the flow of goods from the farmers and importers to the consumers. As

FIGURE 2-B

REBATE FLOWS THROUGH THE FOOD CHAIN



NOTE: Arrows indicate rebate flows.

indicated previously, rebating is insignificant from the farmers' and importers' level to the processors' level. Rebating appears to start at the processors and importers of finished products. The arrows indicate the flow of rebates.

CATALOGUE OF REBATES

The Terms of Reference charge the Commission to inquire into discounts, allowances and rebates.

These are defined in The Shorter Oxford English Dictionary* as follows:

> Rebate - A reduction from a sum of money to be paid;
>
> Allowance - The action of placing to one's credit, admitting in an account, or alloting on account of expenses;
>
> Discount - An abatement or deduction from the amount or from the gross reckoning of anything.

As previously stated, for the sake of brevity and of clarity, I have used the word "rebate" for all three terms throughout this Report.

The consultants, in their survey, found 20 clearly different types of rebates being used in Ontario. These

* 3rd ed. (1978).

are divided into five categories, the first four of which exhibit differing functions, as follows:

ECONOMIES OF SCALE

(i) Volume rebate

(ii) Carload and truckload allowance

ADVERTISING

(iii) Co-operative advertising allowance

(iv) Promotion allowance

(v) Trade allowance

(vi) Display allowance

(vii) Consumer deal

(viii) Store-opening allowance

SERVICE

(ix) Shelf-service/drop-ship allowance

(x) Stale-product allowance

(xi) Quality-control allowance

(xii) Introductory/listing allowance

(xiii) Agents commission/brokerage allowance

(xiv) Pickup/freight allowance

(xv) Warehouse allowance

(xvi) Leaks and swells/leaker/vacuum allowance

(xvii) Inter-canner allowance

(xviii) Label allowance

FINANCE

(xix) Cash discount

(xx) Early-booking discount

MISCELLANEOUS

(xxi) Special allowance

(xxii) Supply contract allowance

NAME BRANDS - HOUSE BRANDS - NO-NAME PRODUCTS

Before dealing specifically with the various kinds of rebates listed above, I should differentiate between name brand, house brand and no-name products.

Name brand products are those which carry a manufacturer's brand name, for example, Campbell soups and Kellogg cereals. House brands are associated with a retailer. There are two types. The original type is the retailer's brand such as Richmello, a trade name of Dominion Stores. The newer type is the no-name product or generic product. This product carries no brand name but is sponsored by a retailer.

As will be seen later in the Report (Chapters 5 and 11), the level of rebate varies for these different types of products.

ECONOMIES OF SCALE

(i) VOLUME REBATE

Volume rebates are payments made to a purchaser as a "reward" for buying a certain quantity of product. Typically, a schedule is published fixing a sliding scale

of rebate levels that ranges generally from 0.5% for small purchases to 5% for large purchases. This means the purchaser at the highest level of the scale receives a refund of up to 5% on his annual purchases. The scale is divided into plateaux, brackets, or steps based on annual dollar purchases, or sometimes on case or tonnage purchases. The payment is typically made by cheque to the purchaser's head office, either quarterly, semi-annually or annually. The dairy industry is an exception in that its payments are much higher than other industries and are often paid on an off-invoice basis. See Chapter 6 for information on milk processors and Appendix 6 for an example of a manufacturer's volume rebate schedule.

An example of volume rebates is as follows. Assume that a retailer buys $1,000,000 of a certain brand name product in a year. Having reached this level of purchases, he may qualify for a 4% volume rebate or $40,000. If the same retailer purchased $1,200,000 of the same product the next year, his annual volume rebate may be 5% or $60,000 as he moves into a higher bracket on the scale.

In cases where both house and name brands are purchased, a different method of calculation may be used. If a purchaser buys $500,000 of name brand product and $100,000 of house brand product from a single supplier, the calculation is usually as follows. The plateau that would apply would be the $600,000 plateau, or say 3%, which represents the total purchases. The payment, however, is based only on the name brand purchases, which is 3% of $500,000 or

$15,000. This system reflects the total volume bought by each purchaser but also reflects the fact that suppliers prefer to sell name brands rather than house brands.

A second type of volume rebate is the volume incentive rebate or buying allowance or bill-back allowance. A customer that purchases a specified amount more than his usual purchase receives an extra rebate. The rebate is generally deducted from the invoice price but it may be offered in the form of free goods. The specified amount is usually only a single plateau that is often inaccessible to the small purchaser. This rebate is also called a "bill-back allowance" in reference to the billing method. The purchaser bills the supplier for the amount due. This type of rebate is usually offered for a short term only.

When this plan is a long-term offering of an incentive rebate, it is called a "volume incentive rebate" or "buying allowance." Here, increases in annual sales are rewarded rather than increases over short periods. In the first example, where the purchases increased from $1 million to $1.2 million, the volume rebate increased from 4% to 5%. The volume incentive rebate or buying allowance would be based on the rate applicable to a 20% growth in purchases. Thus the purchaser may receive an additional 2% volume incentive rebate, for example, because his purchases increased by 20% during the year.

(ii) CARLOAD AND TRUCKLOAD ALLOWANCE

This is an amount paid to purchasers of a specific amount of product, namely a carload or truckload. The shipping-cost savings of a full load accrue to the supplier who, in turn, offers an allowance to the purchaser. This allowance is paid either by deduction from the invoice price (hereafter, this method of payment may be referred to as "off-invoice") or by cheque.

ADVERTISING REBATES

(iii) CO-OPERATIVE ADVERTISING ALLOWANCE

This allowance is paid by suppliers to retailers or wholesalers who conduct programs featuring suppliers' products. The programs range from simple in-store advertising to national advertising and many include display activities or special pricing. The most comprehensive programs are sometimes called Co-operative Merchandising Programs or Promotional Allowances.

The supplier generally specifies that a certain percentage of his sales may be spent on co-operative advertising allowances, usually 1% to 5%. A purchaser may spend, say, 3% of purchases on this advertising activity and be reimbursed for these expenses by the supplier. Payment is usually by cheque.

The major retailers prepare a series of co-operative merchandising programs in the fall of each year. The programs range from in-store featuring to very elaborate media campaigns supported by regional store advertising, end-aisle displays, and other promotional activity. There is a dollar cost related to each program. The supplier then chooses the programs, if any, on which he wishes to co-operate with the retailer. The two agree on which dates the programs will be run for the following year. The supplier thus has some control over the thrust of the advertising program he will present through retailers.

Co-operative allowances are also called "proof-of-performance" allowances because they always require proof of performance to be given by the retailer or wholesaler to the supplier. Typical proof of performance is a "tear sheet." This is the newspaper advertisement that the retailer places featuring the supplier's product. This advertisement is presented by the retailer to the supplier in order to prove that he has performed the advertising service. The supplier pays the retailer after receiving the proof of performance. Further comments on co-operative allowances will be found in Chapter 11, on the subject of cost justification, and an example of a retailer's cooperative advertising programs is printed as Appendix 7.

(iv) PROMOTIONAL ALLOWANCE

Suppliers using this program offer a constant percentage of off-case allowance, an allowance deducted from the regular list price of the case. Such an allowance is

offered throughout the year and is not scaled to the volume purchased. For example, a 2% promotional allowance may be offered to all customers, regardless of the size of their purchases. Usually no proof of performance is required and the supplier assumes that the money will be spent on promotional activities. This allowance is usually paid by cheque.

The name "promotional allowance" is used sometimes to mean co-operative advertising allowance. The critical difference between the two allowances is that the promotional allowance requires no proof of performance while the co-operative advertising allowance requires proof.

A further variation of the promotional allowance is the "over-and-above" or "supplementary" allowance. This is a short-term rebate usually paid by cheque and often initiated at the request of the retailer or wholesaler in excess of the normal promotional activities. When it is not connected to specific volumes of purchases, it is a promotional allowance; otherwise, it is a volume allowance.

(v) <u>TRADE ALLOWANCE</u>

The trade allowance or case allowance is similar to the promotional allowance in that it is usually an amount deducted from the list price of a case. No proof of performance is required. The difference between the trade allowance and the promotional allowance is that the trade allowance is only a temporary allowance expected to

be used to reduce the price of goods to the consumer or to pay for promotional activities. Often the supplier will offer an all-inclusive co-operative merchandising program that will include elements of the co-operative allowances, trade allowances and display allowances (see below). The overlapping terminology causes some problems when trying to compare retailer and supplier data.

A variation of the trade allowance is the buying allowance which reduces prices to buyers in the short term. This allowance is related to volume purchases and is treated in the Volume Rebate section above.

(vi) <u>DISPLAY ALLOWANCE</u>

This allowance is often used with the above three programs in a major marketing campaign. It is intended to compensate for the costs of moving the product to aisle ends, or to bins, and of making displays and signs to display the product to its best advantage.

(vii) <u>CONSUMER DEALS</u>

Suppliers often run contests or games or offer coupons to generate consumer interest in their products. The name "consumer deals" refers to payments made by suppliers to reimburse retailers for costs incurred in running contests or collecting coupons. This program is sometimes combined with display allowances, under the latter's name. As indicated earlier, the topic of coupons, meaning payments made directly to consumers, is not treated in this Report

because the terms of reference direct the Inquiry to "discounts, allowances and rebates...other than payments directly to the consumer." It should be noted in passing that payments by coupons amount to less than 2% of total rebates paid in Canada on food products in 1978, according to a study conducted by A.C. Nielson, Ltd.*

(viii) STORE-OPENING ALLOWANCE

Suppliers offer off-case reductions (reductions from the list price of a case) similar to trade allowances to new stores to help the stores build customer traffic. These reductions allow the new stores to offer more specials in their first weeks or months of operation than would otherwise be the case.

SERVICE

(ix) SHELF-SERVICE/DROP-SHIP ALLOWANCE

This rebate is called the "shelf-service allowance" because it is a payment by suppliers to retailers in lieu of the supplier's stocking the retail shelves. Stocking shelves is a service traditionally performed by suppliers for their retail customers. It is also called the "drop-ship allowance" because the supplier drops the shipment at the customer's back door. One industry in which this payment is commonly made is the bakery industry.

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* As reported in The Globe and Mail, April 9, 1979.

(x) STALE-PRODUCT ALLOWANCE

This allowance is another rebate often offered by suppliers in the bakery industry. Traditionally, the baker offered to replace stale baked goods on the retailers' shelves. Today, when the retailer is obliged to remove stale goods from the shelves, the baker often pays the retailer an allowance to compensate him for these stale products. Rather than pay an allowance for each stale item, the baker pays a fixed percentage, representing an estimate of the amount of stale products expected.

Another version of the stale-product allowance is paid on seasonal goods like Christmas cake or its ingredients. These products are offered under terms providing retailers with compensation if the products remain unsold after the end of the season. Alternatively, suppliers offer to take delivery of all unsold products at the end of a specified time period.

(xi) QUALITY-CONTROL ALLOWANCE

On house brand products especially, some retailers perform quality-control services. These services are performed either in-store or in the factory. This service is paid for by suppliers in the form of a quality-control allowance.

(xii) INTRODUCTORY ALLOWANCE/LISTING ALLOWANCE

Retailers are paid by suppliers for the costs and risks incurred by retailers of listing a new product. These costs have been itemized by retailers as follows:

- product examination and acceptance
- inventory list changes
- stock and shelf re-adjustments
- printing of shelf signs
- delisting of other products.

Most suppliers treat this item as either a trade allowance or a promotional allowance. None of the retailers and few suppliers were able to quantify the exact amount paid because their accounting systems do not segregate this information.

The merits of this allowance are discussed in Chapter 15, Listing and Delisting.

(xiii) AGENTS' COMMISSION/BROKERAGE ALLOWANCE

Frequently, the supplier sells his goods through a broker or agent. The broker/agent is paid for performing merchandising services that the supplier must otherwise perform himself. This allowance is offered to the broker usually in the form of a deduction from the invoice price, where goods are purchased by the broker, or in the form of a cheque, where the agent does not purchase the merchandise. This rebate is generally a flat percentage fee that usually does not vary with quantity.

(xiv) PICKUP/FREIGHT ALLOWANCE

Where the buyer pays the expense of shipment or ships the goods himself, the supplier rebates this cost on a fixed-percentage basis to the buyer provided the normal terms of trade include delivery by the supplier.

(xv) WAREHOUSE ALLOWANCE

When a buyer warehouses the goods he bought, the supplier will offer a warehouse allowance. The buyer is performing a storage and re-distribution service and is paid either by reduction from the invoice price or by cheque.

(xvi) LEAKS AND SWELLS/LEAKER/VACUUM ALLOWANCE

The leaks and swells allowance is a small allowance offered by canners to cover the cost of any cans which may be damaged before arrival at the buyer's establishment. Leaker and vacuum allowances are similar allowances for plastic-wrapped meats and vacuum-packed meats. This allowance is set at a fixed percentage based on the average amount of damaged goods that may be expected in a shipment. This allowance is paid off-invoice and is similar to the stale-product allowance described above.

(xvii) INTER-CANNER ALLOWANCE

Often one canner will ask another canner to can a certain quantity during the peak of the season. The second

canner will sell this quantity to the first at a discount. This allowance represents payment for the selling expense saved by the second canner. The allowance is usually deducted from the invoice price.

(xviii) LABEL ALLOWANCE

A buyer sometimes supplies labels to a canner. When this happens, the allowance is granted to the buyer to reimburse the buyer for the cost of label design and manufacture.

FINANCE DISCOUNTS

(xix) CASH DISCOUNTS

The vast majority of suppliers offer a reduction from an invoiced amount if payment is made before a specified time period elapses. The period is usually ten to fifteen days. The supplier gives this allowance to encourage prompt payment of accounts which is advantageous to the supplier's cash flow.

(xx) EARLY-BOOKING DISCOUNT

This discount is offered by some suppliers when orders are booked a specified time in advance of delivery. The advantage to the supplier is that he is able to arrange credit more easily and to plan production with more accuracy. This discount is most often found in the canning

industry, and is usually paid by deducting a percentage from the invoice price.

MISCELLANEOUS

(xxi) SPECIAL ALLOWANCE

This allowance is most often encountered on house brand products. It is usually paid to the buyer for a range of services including label design, quality control, warehousing and brokerage. Although this allowance has been classified separately because of the method of calculation, the functions, which may vary in each case, are identical to those of the rebates described above. The buyer accepts a price and then asks the supplier to raise the price by x per cent and to refund the same x per cent to the buyer. The net price to the supplier remains the same. This allowance has generated suspicion among the suppliers because adequate explanation for the purpose of the allowance is seldom given.

Buyers favour this type of allowance because they receive a separate cheque for the services they provide. Consequently, they are able to apply the revenue from the cheque directly against the expenses incurred in providing the service.

(xxii) SUPPLY CONTRACT

This is an infrequently encountered rebate that consists of a supplier paying an amount for the right to

supply a customer. This is a rebate because it represents a payment related to goods sold. It is a form of volume rebate because it is applied to the customer's purchases over the duration of the contract.

NON-MONETARY BENEFITS

In addition to the various types of rebates that have already been listed, retailers also receive from suppliers certain non-monetary benefits. Our consultants were unable to quantify these as their surveys were directed to monetary rebates.

The evidence indicated a variety of benefits such as:

1. Financial assistance is given to small retailers in the purchase of refrigeration equipment. Canada Packers, for example, will provide a freezer for ice cream if the customer wishes, and the cost is amortized in the ice cream price. Donlands Dairy will sell a refrigerator to an independent retailer and allow him time to pay for it at a lesser rate of interest than the rate charged by banks.

2. Certain suppliers are prepared to stock the shelves of retailers without charge. This does not occur in the larger chains which are unionized and which have collective agreements prohibiting stocking. Certain of the larger chains are also opposed to shelf stocking for security and

management control reasons. Shelf stocking by suppliers generally takes place in non-unionized independent retail stores.

3. It is a common practice for certain suppliers to offer guaranteed sales. That is, if the product is not sold by the retailer, the supplier will take back the unsold portion. The type of merchandise usually sold in this manner is a product that has a short selling period. Another type is the "fad" item, a portion of which will not likely sell at a regular retail price within the selling life span of the product. Examples of these types of merchandise are highly seasonal items such as Valentine's Day products, Easter eggs and Hallowe'en candy.

BREAKDOWN OF EXPENDITURE BY REBATE GROUP

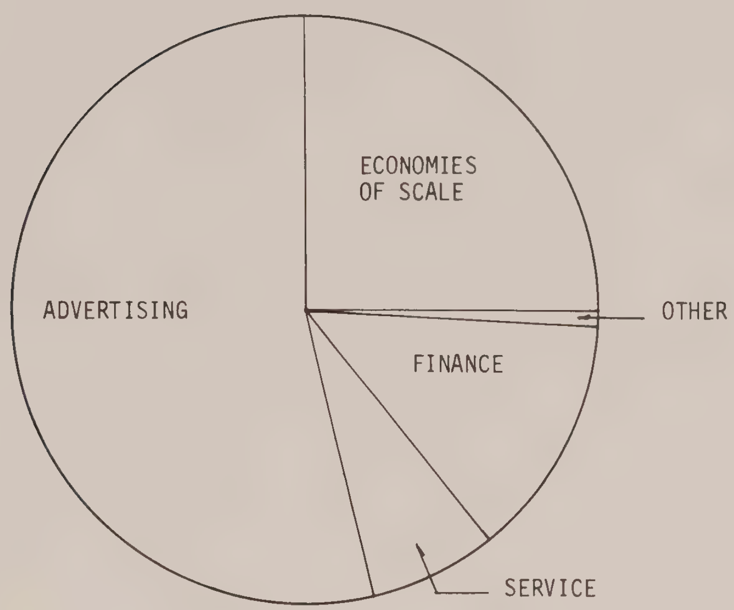
Having divided rebates into five major groups, I will now consider the relative dollar expenditure by processors for each group. This is shown in Figure 2-C.

Figure 2-C indicates that the expenditure on advertising represents 57.8% of the total expenditures of all rebates. Economies of scale are next in size at 25.3% and then there is a pronounced decline to finance at 12.0%.

Advertising and economies of scale rebates total 83.1% of all rebate expenditures.

FIGURE 2-C

BREAKDOWN OF EXPENDITURE BY REBATE GROUP



Economies of Scale	25.3%
Advertising	57.8%
Service	4.8%
Finance	12.0%
Other	0.1%
TOTAL	100.0%

Source: Processor/Manufacturer Questionnaire

FREQUENCY OF USE OF REBATE TYPES

Table 2-A shows the differing patterns of use of rebates for name brand and house brand products. Each column totals more than 100% because processors use several types of rebates for their products.

In considering the table, one must realize that certain specialized rebates are associated predominantly with certain kinds of products, as shown below.

REBATE	PRODUCT
Stale-Product Allowances	Baked Goods
Shelf-Service Allowances	Baked Goods
Leaks and Swells Allowances	Canned Goods
Vacuum/Leaker Allowances	Packaged Meats
Early-Booking Discounts	Vegetable and Fruit Canning
Inter-canner Allowances	Vegetable and Fruit Canning

AVERAGE SIZE OF REBATES PAID

The average amount of each rebate expressed as a percentage of payment relative to total sales of processors is shown on Table 2-B.

Column 2 provides the common range of this percentage. The common range excludes certain anomalous data such as dairy products because the inclusion of this data would

TABLE 2-A

FREQUENCY OF USE OF REBATE TYPES

Rebate Type	Frequency on Name Brands	Frequency on House Brands	Frequency Over-all
Volume rebates	67.1%	25.5%	70.1%
Carload/truckload discount	10.6%	1.8%	11.5%
Co-operative allowance	71.8%	7.3%	70.1%
Promotional allowance	28.2%	5.5%	28.7%
Trade/display allowance	61.2%	20.0%	60.9%
Consumer deals	1.2%	---	1.2%
Store-opening allowance	2.4%	---	2.3%
Shelf-service/drop-ship discount	7.1%	3.6%	6.9%
Quality-control allowance	---	---	---
Listing/introductory allowance	5.9%	---	5.8%
Agent/broker allowance	5.9%	9.1%	10.3%
Pickup/freight allowance	3.5%	1.8%	3.4%
Warehouse allowance	11.8%	1.8%	12.6%
Leaks and swells allowance	12.9%	21.8%	16.1%
Inter-canner discount	3.5%	1.8%	3.4%
Label allowance	1.2%	1.8%	1.2%
Cash discount	72.9%	70.9%	75.9%
Early booking discount	4.7%	3.6%	6.9%
Special allowance	---	14.6%	9.2%
Supply contract	1.2%	---	1.2%

NOTE: 1. Frequencies are defined as the proportion of suppliers using the rebate type out of all those selling name or house brand products. The over-all frequency represents the proportion of suppliers in the entire sample who used the rebate type for a name brand, house brand, or both.

2. Quality-control allowance is not offered for name brand products. House brand quality-control allowance is paid through special allowances.

3. Figures include off-invoice amounts.

SOURCE: Processor/manufacturer questionnaire.

TABLE 2-B

AVERAGE SIZE OF REBATE PAYMENTS

Rebate Type	Average Size (% of sales)	Common Range (% of sales) Low	High
Volume rebates	3.2	0.3	6.0
Carload/truckload discount	0.7	0.1	1.2
Co-operative allowance	3.4	0.3	6.0
Promotional allowance	3.4	1.2	5.0
Trade/display allowance	4.2	1.0	8.0
Consumer deals	---	---	---
Store-opening allowance	---	---	---
Shelf-service/drop-ship discount	2.6	1.5	5.0
Quality-control allowance	---	---	---
Listing/introductory allowance	1.8	---	---
Agent/broker allowance	2.1	1.0	3.0
Freight allowance	3.3	2.0	3.0
Warehouse allowance	0.8	0.3	1.7
Leaks and swells allowance	0.3	0.1	0.2
Inter-canner discount	1.7	---	---
Label allowance	1.3	---	---
Cash discount	1.4	1.0	2.0
Early booking discount	0.9	0.5	2.5
Special allowance	---	---	---
Supply contract	---	---	---

NOTE:

1. Store-opening allowances and consumer deals have been reported in trade allowances.
2. Special allowances, supply contracts and quality-control allowances were not reported frequently enough to yield meaningful averages or ranges.
3. Listing allowances, inter-canner discounts, and label allowances were not reported frequently enough to yield meaningful ranges.
4. Figures include off-invoice amounts.

SOURCE: Processor/manufacturer questionnaire.

present an unbalanced picture. Rebates in dairy products are dealt with separately in Chapter 6.

The typical processor offers three to five rebates and co-ordinates their use with his marketing strategy and his resources.

REBATE LEVEL BY PRODUCT GROUP

Table 2-C sets out the amount of rebates by product category. The percentages indicated represent an average; there can be a wide divergence in a product group. For example, the dairy processors offer from 5% to 30%.

The rebates are calculated as a ratio of rebate payments to net sales by processors. Within each product group, the products are ordered from highest to lowest rebate level. Spices, for example, have higher average rebates than coffee and tea.

OFF-INVOICE ALLOWANCES

One of the major difficulties faced by the Inquiry was the ascertainment of the value of off-invoice allowances. As noted previously, the term "off-invoice" refers to the method of payment of the rebate. An off-invoice allowance is paid by a reduction in the amount shown on the face of the invoice. For example, a retailer may purchase 100 cases of goods at $15 per case. When the merchandise is purchased, a trade allowance is offered which reduces the price of goods by $1 per case, and which is paid by the

TABLE 2-C

REBATE LEVEL BY PRODUCT GROUP

Product Group	Rebate Percentage
Dairy (exclusive of cheese products)	20%
Spices Coffee and tea Soft drinks Bread Frozen Foods	14% to 10%
Oils Sauces and Gravies Other Baked Goods Fish Sugar Candy	9% to 7%
Soups Meats Canned Fruit and Vegetables Cereal products Cheese products	6% to 4%

NOTE: 1. Rebates are calculated as the ratio of rebate payments to net sales by processors. This is comparable to the ratio of rebate receipts to net purchases by retailers.

2. Includes off-invoice amounts.

SOURCE: Processor/manufacturer and retailer questionnaires.

off-invoice method. The invoice received by the retailer shows the $1,500 total price less $1 per case for 100 cases, yielding a net price of $1,400. The retailer pays $1,400 to the seller.

The major reason for the difficulty in calculating the exact amount of off-invoice allowances is the accounting system used by the large majority of retailers. The retailers' books of account show that the purchase price of the goods in the example above is $1,400 which is the amount the retailer actually paid for the goods. Because no running total is kept of the gross cost (in this example, $1,500) or of the off-invoice allowance ($100), retailers do not know the exact amounts. On the other hand, rebates received by retailers that are paid by cheque are all fully recorded as income.

Processors account for all rebates, whether paid by off-invoice or other methods. These rebates are usually classified as selling expenses.

In order to arrive at a figure that expresses the average rebate received by retailers, the rebates paid by processors were compared with the rebates received by retailers. Faced with the impossibility of obtaining an exact figure, the Commission asked the various retailers to provide an estimate of their off-invoice allowances. This involved a great deal of effort and expense on their part and I am appreciative of their cooperation. Rebate levels are reported and discussed in Chapter 5 on processor/-

manufacturers and rebates, and in Chapter 9 on large retailers.

CONCLUSIONS

The following summarizes my conclusions as to the evidence examined in this chapter:

1. The system of discounting presently existing in Ontario is a rational and regular method of marketing food products benefitting both processor and retailer. Its effect on the farmer and on the consumer will be considered in subsequent chapters.

2. Rebates are paid almost exclusively by sellers of processed and manufactured goods to wholesale and retail buyers.

3. There are twenty distinct types of rebates which can be categorized into five functionally distinct groups of rebates that are listed in order of importance: advertising, economies of scale, finance, service and miscellaneous.

4. Each group of rebates serves a general purpose in the processor/manufacturer's marketing program. Advertising rebates generally pay for co-operative efforts designed to promote food products. Economies-of-scale rebates generally recognize economies realized by volume sales of these

products. Finance rebates generally invite terms of payment favourable to the seller's finances. Service rebates generally encourage the buyer to provide services in connection with the sale and distribution of these products.

5. Rebate amounts differ depending on the product group. Rebate amounts paid on the sale of dairy goods are much higher than on the sale of any other product group. For this reason, dairy rebates are considered separately in Chapter 6, Milk Processors and Rebates.

6. In addition to rebates received in the form of payment by cheque, retailers receive rebates in the form of reductions from invoiced amounts called "off-invoice allowances." Off-invoice allowances are not generally recorded as separate items in accounting records and therefore must be estimated. All references to rebates in this report include off-invoice allowances, except where these allowances are specifically excluded.

CHAPTER 3

EFFECT OF REBATES ON FARMERS

EFFECT OF REBATES ON FARMERS

GENERAL

A major term of reference for the Inquiry to answer is the effect of rebates on the farmer.

There are two aspects to this problem. The first aspect concerns rebates paid by a farmer on the sale of his products. This aspect is dealt with in this chapter. The second aspect concerns the broader allegation raised by the Ontario Federation of Agriculture that the system of rebating concentrates buying power for farm products, adversely affecting the farmer. This aspect is dealt with in Chapter 13, Concentration and Rebates.

The conclusions reached in this chapter are based on evidence heard at the Inquiry, interviews with farmers and organizations representing farm interests, and research by the consultants.

HOW DOES THE FARMER SELL HIS PRODUCTS?

In order to ascertain whether or not rebates are paid by farmers, it is necessary to understand the complex systems by which farm products are sold in Ontario.

Simply stated, farm products are either subject to marketing board regulation or not subject to marketing board regulation. Ontario farm cash receipts from farming

operations amounted to $2.86 billion in 1977. Figure 3-A shows that 57% of the total receipts were on the sale of products subject to marketing board regulation. This amounted to $1.63 billion. Figure 3-A further indicates that 43% of the total receipts were on the sale of products not subject to marketing boards. This amounted to $1.23 billion. Figures from 1977 are used throughout because they were the latest complete figures available at the time of writing.

Based on informal estimates by Ministry of Agriculture and Food personnel, it appears that the proportions of sales of regulated and non-regulated products will be approximately the same for the years 1978-1980.

Table 3-A is a breakdown of the value of various product sales according to whether or not they are subject to a marketing board. The marketing system used is significant from the standpoint of rebates. For this reason, the following paragraphs will deal with the products separately as to the method of sale.

FORMATION OF A MARKETING BOARD

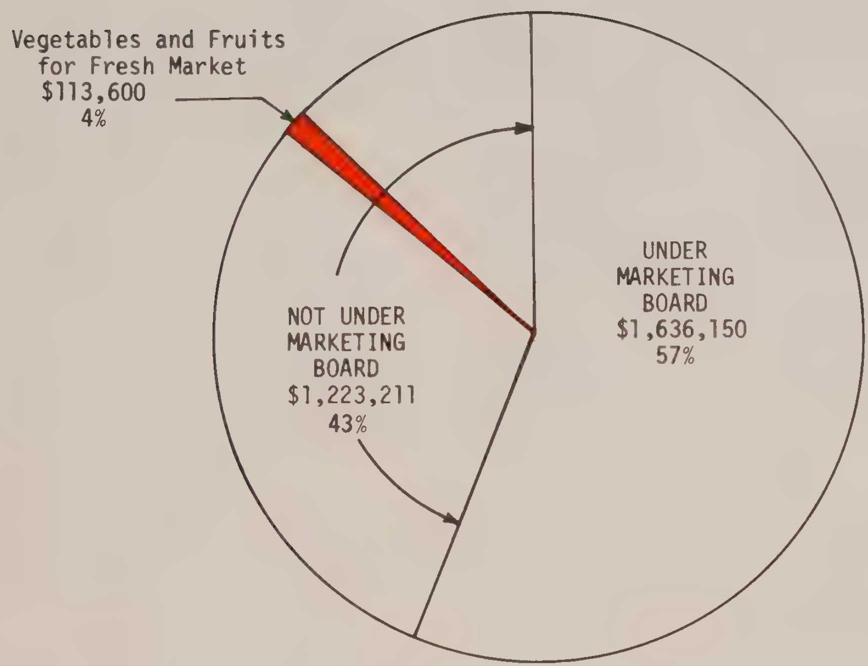
The formation and administration of a marketing board is governed by The Farm Products Marketing Act, (R.S.O. 1970, c. 162, as amended).

The impetus for the formation of a board must come from a group of producers. At least fifteen per cent must sign a petition or request and forward it to the Farm

FIGURE 3-A

ONTARIO FARM CASH RECEIPTS - 1977

($000's)



SOURCE: Ontario Ministry of Agriculture and Food

TABLE 3-A

ONTARIO FARM CASH RECEIPTS
1977

Product	Total	Under Marketing Board	Not Under Marketing Board
		- $'000 -	
Wheat	84,200	84,200	--
Oats	1,370	--	1,370
Barley	5,280	--	5,280
Rye	151	--	151
Soybeans	78,700	78,700	--
Corn	153,000	--	153,000
Tobacco	173,000	173,000	--
Other Crops(1)	183,000	9,150	173,850
TOTAL FIELD CROPS	678,701	345,050	333,651
Cattle and calves	668,000	--	668,000
Hogs	291,000	265,000	26,000
Sheep & Lambs	4,960	--	4,960
Dairy Products	512,000	512,000	--
Poultry	175,000	169,000	6,000
Eggs	107,000	92,000	15,000
Other livestock & products(2)	33,000	--	33,000
TOTAL LIVESTOCK & LIVESTOCK PRODUCTS	1,790,960	1,038,000	752,960
Fruits:			
- for processing	14,171	14,171	--
- for fresh market	54,829	41,829	13,000
TOTAL	69,000	56,000	13,000
Vegetables: (including potatoes & mushrooms)			
- for processing	75,700	75,415	285
- for fresh market	102,100	--	102,100
- greenhouse vegetables	14,900	14,900	--
TOTAL	192,700	90,315	102,385
Other Cash Receipts(3)	128,000	105,000	23,000
GRAND TOTAL	2,859,361	1,634,365	1,224,996

NOTE: 1. Includes floriculture and nursery products, dry beans and other minor crops.
2. Includes wool, honey, fur, farming and other minor livestock.
3. Includes forest and maple products, provincial income, stabilization payments, deficiency payments, and dairy supplementary payments.

SOURCE: Economics Branch, Ontario Ministry of Agriculture and Food.

Products Marketing Board, which is established by the Act. If the Board is satisfied that the group of producers is representative of the persons engaged in the production of the particular farm product, it may recommend the establishment of a plan to the Minister of Agriculture and Food.

The Minister may then authorize an opinion poll of the producers that would be affected by the plan. The poll is supervised by an independent person. If the result indicates to the Board a representative group is interested in the plan, and if the plan is within the intent of the Act, the Board may recommend to the Minister the formation of the plan. The Minister, if in agreement, recommends the plan to the Cabinet for implementation.

PRODUCTS REGULATED BY MARKETING BOARDS

The basic objectives of marketing boards are to obtain a fair return on the sale of farm products and to arrange an orderly system of marketing. The Board offers a system of collective bargaining to the producer for marketing his product.

Ontario has developed, over many years, a unique system of marketing boards. The boards are not universally popular with producers, processors, and retailers. The evidence indicated that some producers and processors are opposed to marketing boards as they represent a restriction of free enterprise. Certain retailers felt that products subject to boards are over-priced.

There are 23 marketing boards operating in Ontario involving more than 40 farm products. Twenty-one operate under The Farm Products Marketing Act and two under The Milk Act, (R.S.O. 1970, c. 273), one for milk and one for cream.

There are four main categories of boards:

(a) boards that promote and develop the regulated product;

(b) boards that negotiate price;

(c) boards that establish price;

(d) boards that regulate production or marketing quotas.

Six of the boards establish price agreements through the mechanism of negotiating committees on which board members and customers are both represented. If negotiation fails, arbitration is available. Nine boards establish price after evaluating market place conditions and after consultation with the industry. Seven boards negotiate or establish prices while regulating production and marketing quotas, in order to provide a balance between supply and demand. One board is limited to research and market development. Another board is inactive and, therefore, is not included in the number of operating boards.

The functions given to each board differ from board to board. The boards charge license and service fees to their members intended to defray the cost of operation of the boards.

Farmers may take complaints concerning fees to their marketing board, and if not satisfied, may appeal to the Farm Products Appeal Tribunal. The Appeal Tribunal is composed of farmers and non-farmers and is chaired by a person from the Ministry of Agriculture and Food.

The various boards and their functions (excluding boards governing tobacco crops) are as follows:

BOARDS THAT DEVELOP AND PROMOTE THE REGULATED PRODUCT	FUNCTIONS
Fresh Potato Growers' Marketing Board	Promotes industry through research, quality improvement and market development. Represents Ontario producers on the Eastern Canadian Potato Producers' Council. Provides marketing information to producers.

BOARDS THAT NEGOTIATE PRICE	FUNCTIONS
Berry Growers' Marketing Board	The Berry Board is currently inactive although it does participate in the promotion of strawberries.

Grape Growers' Marketing Board (Processing)	Negotiates prices with processors and wineries for 16 classes of grapes. Establishes terms and conditions for sale by regulation. Buyers contract directly with growers, with payments to the grower made through the board. Promotes the sales of Ontario wine and grape juice products.
Potato Growers' Marketing Board (Processing)	Negotiates prices, grades and terms and conditions of sale for potatoes contracted for processing into french fries, soups and stews, pre-peeling, chips and dehydrated products. Administers a two-tier pricing system, permitting the purchase of a limited quantity of potatoes indexed to the Table Stock Market.
Processing Tomato Seedling Plant Growers' Marketing Board	Negotiates price, grades and terms and conditions of sale for Ontario grown tomato plants.
Seed Corn Growers' Marketing Board	Negotiates price, terms and conditions of sale, and

	charges related to contracts for seed corn production in Ontario.
Soya Bean Growers' Marketing Board	Negotiates minimum price for soybeans based on the delivered price of U.S. soybeans and the charges for cleaning, handling and drying by dealers. Establishes the terms and conditions of sale by regulation. Promotes and develops a market for soybeans for human consumption and export.
Vegetable Growers' Marketing Board (Processing) Green and wax beans, lima beans, red beets, cabbage, carrots, peppers, cauliflower, sweet corn, cucumbers, green peas, pumpkin, squash, and tomatoes	Negotiates prices, grades and terms and conditions of sale for 14 vegetables grown for processing. Regulates all agreements entered into between producers and processors. Administers by regulation term contracts. Processors contract directly with individual growers. Co-operates in commitees for specific commodities to improve quality and promote consumption.

BOARDS THAT ESTABLISH PRICE	FUNCTIONS
Apple Marketing Commission	Establishes prices to wholesale and retail buyers. Promotes apple sales by collection of license fees from producers on an acreage basis.
Asparagus Growers' Marketing Board	Establishes prices, grades and terms and conditions of sale for asparagus for processing. Processors may contract asparagus directly or purchase asparagus through the board. Promotes marketing of fresh and processed asparagus. Contributes to the development of new asparagus varieties for Ontario.
Bean Producers' Marketing Board	White Pea Beans. Markets through its appointed agents all beans delivered to elevators and stored for the board. Offers for sale by tender a specific quantity and price in light of domestic and foreign competition. Pools returns from sales and pays to the growers the price received

	for the beans less service charges and license fees.
	<u>Yellow Eye Beans</u>. Establishes prices. Determines annual marketing quotas. Pools returns for payment to the growers.
Fresh Grape Growers' Marketing Board	Establishes prices, variety, grade and terms and conditions of sale for grapes sold on the fresh market. Conducts sales through appointed agents. Promotes the consumption of fresh grapes.
Greenhouse Vegetable Producers' Marketing Board	Establishes prices and appoints agents for the sale of greenhouse tomatoes and cucumbers. Pools separate weekly returns from sales for each of the seven agents in the Leamington district and pays growers the price less service charges and license fees. Introduces and promotes the use of seedless cucumbers.
Pork Producers' Marketing Board	Operates marketing yards throughout Ontario and sells

	live hogs on a graded basis through a teletype auction. Pools return to growers weekly from auction sales. Supplies hogs for shipment to export market by contract to packers. Promotes sale of pork with emphasis on quality and nutritional value of Ontario pork.
Rutabaga Producers' Marketing Board	Establishes prices and terms and conditions of sale. Appoints agents to market rutabagas. Promotes the consumption and export of rutabagas.
Tender Fruit Producers' Marketing Board (peaches, pears, plums and cherries)	Establishes prices, grade, variety and terms and conditions of sale for tender fruit sold for processing and the fresh market. Processors contract directly with individual growers, with all payments to the growers made through the board. Operates a Central Fruit Exchange in the Niagara Peninsula and appoints agents for the sale of fresh fruit. Promotes the consumption of tender fruit.

Wheat Producers' Marketing Board	Conducts through its appointed agents all sales of Ontario produced wheat. Establishes a domestic wheat price under the Federal Two-Price Wheat Act. Determines export prices in response to international market conditions. Pools returns from sales and pays to growers the price for the wheat less all service charges.

BOARDS THAT REGULATE WITH PRODUCTION AND MARKETING QUOTAS	FUNCTIONS
Chicken Producers' Marketing Board	Allots production quotas to producers and after consultation with processors, feed manufacturers and hatcheries allocates marketing quotas to meet demands for broiler and roaster chickens. Establishes weekly prices for broiler and roaster chickens. Participates in the Canadian Chicken Marketing Agency.

Cream Producers' Marketing Board	Negotiates price of farm separated cream with processors. Participates in a National Milk Supply Management Program for Industrial Milk. Allocates provincial quotas to producers.
Egg Producers' Marketing Board	Participates in the Canadian Egg Marketing Agency which establishes the price of Grade A eggs according to a cost-of-production formula. Allots the Ontario share of the national quota by regulating the hen numbers to individual producers holding production quota. Promotes the consumption of eggs.
Milk Marketing Board	Buys all milk sold off the farm in Ontario and sells it to dairies and processing plants. Establishes prices to processors by regulation. Participates in a National Milk Supply Management Program for Industrial Milk. Allocates provincial quotas to producers.

Turkey Producers' Marketing Board	Participates in the Canadian Turkey Marketing Agency. Establishes prices according to a cost-of-production formula. Allots Ontario's share of the National Marketing quota to producers holding production quotas. Promotes the consumption of turkey.*

Based on the evidence given at the Inquiry, it may be stated conclusively that producers subject to a marketing board do not encounter rebating on their products without the knowledge and approval of their board, or, if they do, both parties to the transaction are subject to legal penalty. The Board gives its approval to certain rebates included in the contract. Otherwise, it is illegal for a producer or buyer to vary from the price established by a marketing board pursuant to Section 16 of The Farm Products Marketing Act. I have quoted below the relevant portion of this section:

> "Every person who fails to comply with or contravenes any of the provisions of this Act...or of any plan, or of any order, regulation or

* The information in this section is taken from Ontario Ministry of Agriculture and Food, Ontario Agricultural Marketing Boards - 1980, (Farm Products Marketing Branch: March, 1980).

direction of the board or any local board or of any agreement or award or renegotiated agreement or award filed with the board, is guilty of an offence...and is liable for a first offence to a fine of not more than $500 and for a subsequent offence to a fine of not more than $5,000."

The various marketing boards monitor their own marketing systems. All boards have professional managers and in some cases, inspectors.

PRODUCTS NOT REGULATED BY MARKETING BOARDS

As previously stated, farm cash receipts for products not subject to marketing boards totalled $1.22 billion in 1978, or 43% of the total receipts for all farm products in that year.*

The producers of these non-marketing board products, for various reasons, prefer to market their products in their own way. One can only conclude that they feel their needs are better met in this way than by the formation of a marketing board.

The major commodity groups not under marketing boards are: livestock, field crops, fresh vegetables and fresh fruit. Figure 3-B indicates the percentages of total sales not subject to market board regulation represented by these groups of commodities.

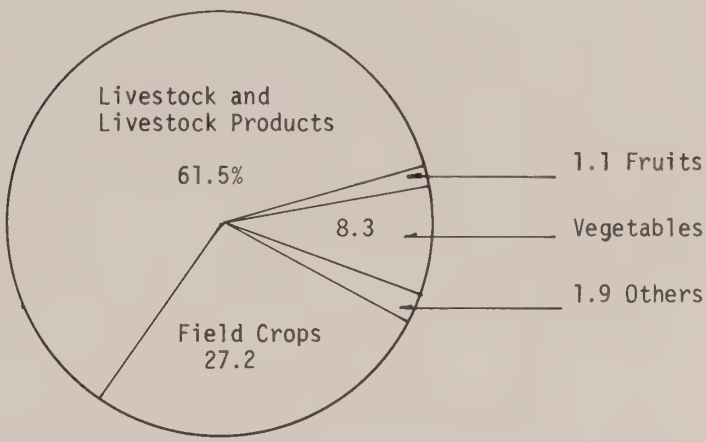
* All figures in this section are from estimates by the Economics Branch, Ministry of Agriculture and Food, October 22, 1979.

FIGURE 3-B

BREAKDOWN OF ONTARIO FARM CASH RECEIPTS
NOT SUBJECT TO MARKETING BOARD REGULATION, 1977

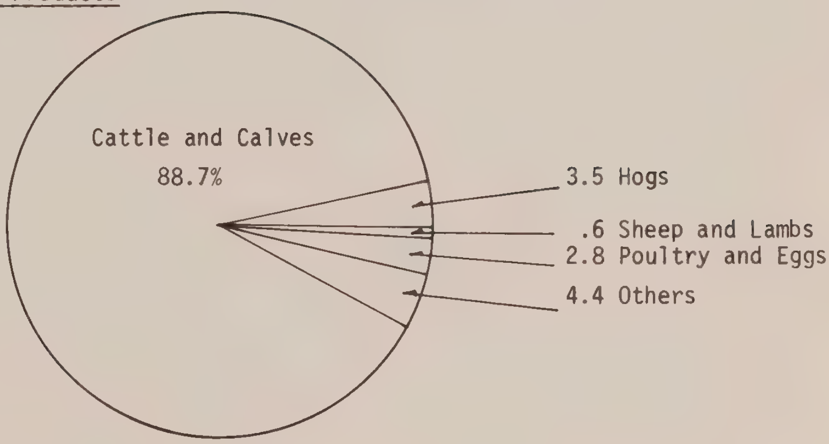
All Commodities

By Major
Commodity Groups



Livestock and Livestock Products

By Specific Classes
of Livestock



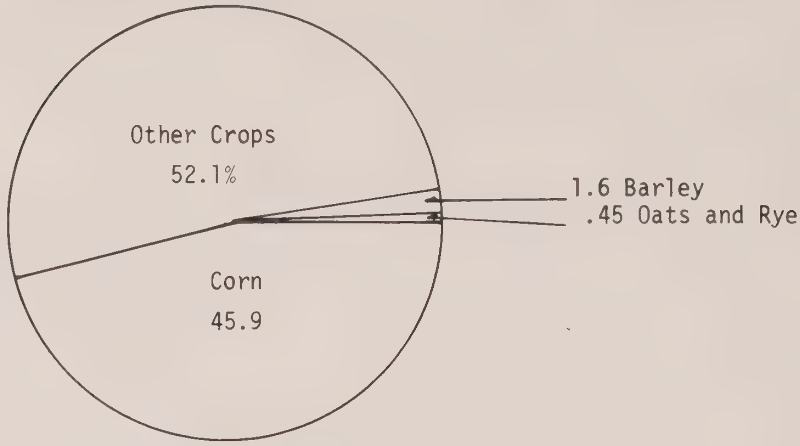
SOURCE: Ontario Ministry of Agriculture and Food

FIGURE 3-B

BREAKDOWN OF ONTARIO FARM CASH RECEIPTS
NOT SUBJECT TO MARKETING BOARD REGULATION, 1977
(Continued)

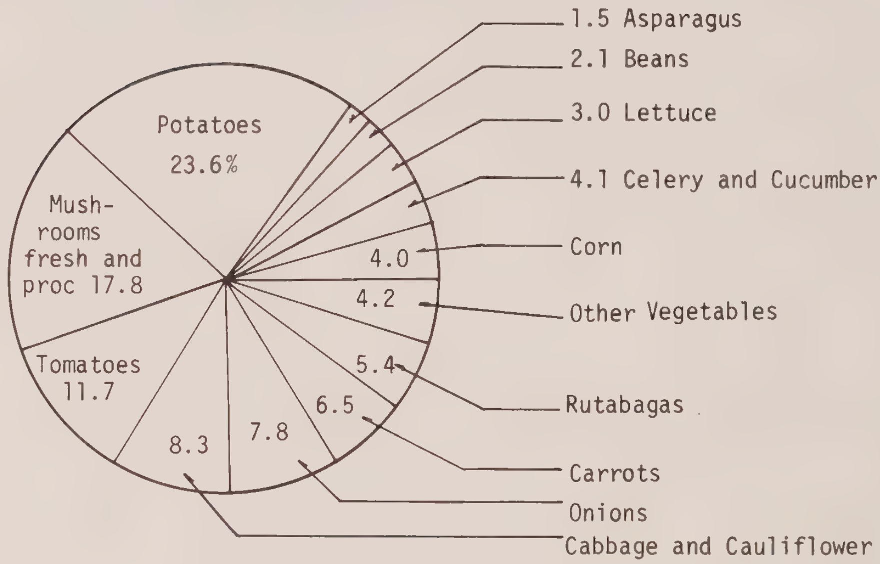
Field Crops

By specific crops



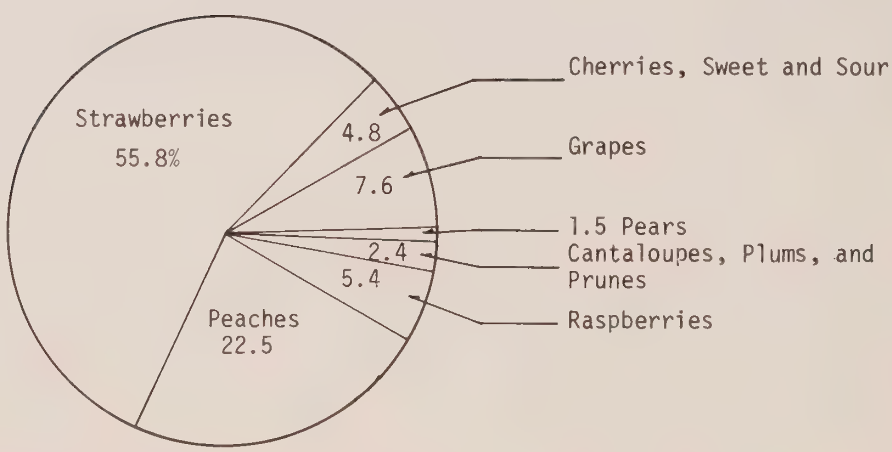
Vegetables, Fresh

Proportion of specific vegetables



Fruits, Fresh

Proportion of specific fruits



SOURCE: Ontario Ministry of Agriculture and Food

These results may be summarized as follows for the major groups:

Livestock and livestock products	61.5%
Field crops	27.2%
Vegetables	8.3%
Fruits	1.1%

I shall now consider the sale of each of these major groups.

A. LIVESTOCK

The two major meats sold in Ontario are beef and pork. Lamb is sold in much less volume as indicated in Figure 3-B which shows the breakdown of sales for the livestock group. This figure shows that sales of cattle and calves dominate this category. It should be noted that these are 1977 figures and there would likely be some variation as consumers increased their purchases of pork in 1978-1980 due to the high price of beef.

Beef cattle producers operate on a well-organized competitive open-market system, with several options. Producers are aware of current market prices. Of the approximately 1,370,000 head sold, approximately 30% is sold at the large public auctions in Toronto and Kitchener. Another 30% is sold through 70 community auction barns while 35% is sold directly to meat packers on a live or dressed basis. Approximately 5% is exported. These totals exclude small numbers of cattle slaughtered on the farm for home consumption.

Based on the Commission staff's interviews with farmers and Ministry of Agriculture and Food personnel and based on the lack of complaints to this Commission, there does not appear to be systematic rebating in beef cattle sales.

Hogs are sold under a marketing plan establishing the Ontario Pork Producers Marketing Board. This Board does not fix prices; the hogs are sold under an advanced system of teletype sales, known as the Dutch clock system. All hog sales are conducted by the Board on Dundas Street in Toronto where producers' bids are received by an electronic bidding system.

The Dutch auction principle is to start at a high price and proceed to a low price. Thus, the Dutch auction clock is started at the maximum likely price. The price on the clock starts coming down. Buyers receive prices and communicate bids by teletype. If a buyer is willing to accept the price indicated, he places a bid which stops the clock, and he becomes the buyer. The bidders present are meat packers and processors; retailers do not take part in the bidding.

This is a simple explanation of how the system operates. Over 90% of Ontario pork is sold pursuant to the system described above. There was no evidence nor did my investigations indicate that the remainder is subject to systematic rebating. It is sufficient to indicate that purchasing pork is on a strictly competitive basis, in which rebating plays no part.

A Dutch auction system also exists for veal calves on the Toronto market. Lamb, like beef, is sold by auctioneers. Therefore, I conclude that rebating is not a factor in sales of these commodities, either.

B. FIELD CROPS

Field crops not subject to marketing board regulation consist of oats, barley, rye, corn and other crops. These crops represent 27.2% of all non-marketing board produce sales.

1. CORN

Corn represents 45.9% of all field crops not sold under marketing boards. One type of corn, field corn, is used for animal feeds, the major buyers being the elevators and feed mills of Ontario. A small amount is sold to export markets and the sales are usually made by elevator operators rather than producers.

Another type of corn, sweet corn, is used for human consumption, and is dealt with under the heading of Vegetables which follows.

The field corn market is well organized; pricing information is widely disseminated. There are no retail chain buyers in this market. There was no evidence nor did my investigations indicate any systematic rebating in respect of this crop.

2. BARLEY, OATS AND RYE

These crops represent 2.1% of the field crop group. Sales are generally handled by grain elevator and mill operations. Market conditions for the sale of these crops are similar to the field corn market outlined above.

There was no evidence nor did my investigations indicate any systematic rebating in respect of these crops.

3. OTHER FIELD CROPS

The bulk of this category is floriculture and nursery products and includes small amounts of dry beans and other food crops.

Floriculture and nursery products are outside the terms of reference of this Commission. The other crops in this category are treated on the whole as the field corn crop.

There was no evidence nor did my investigations indicate any systematic rebating in respect of these crops.

C. VEGETABLES

Fresh vegetables are those sold for fresh consumption as opposed to processed consumption. The vast majority of vegetables sold for processing purposes are sold under marketing board jurisdiction.

Fresh vegetables account for 8.3% of the value of produce not under marketing board jurisdiction, and

approximately 3.4% of all farm produce.

The individual grower may truck his produce to Toronto for sale at the Ontario Food Terminal, an open market conducted on a cash basis. If the grower chooses to sell in this manner, he takes his chances as to price and as to whether or not he will be able to sell his load.

The grower may also sell to retail outlets, supermarkets, produce retailers or to operators of roadside stands. He may also sell directly to the consumer at the grower's own roadside stand.

Still another way a grower may sell is to a group selling agency or through a group selling agency. In the case where he sells to a selling agency, the price is agreed upon by the grower and the agency after the latter receives the shipment. The agency then assumes the responsibilities and costs of reselling the produce. Where produce needs further attention, it is a matter of agreement as to price depending on what services will be performed.

In the case where the farmer sells through a group selling agency, the usual arrangement is that the agency pays the farmer the amount received from the sale of the produce less a brokerage fee for the selling services performed. If the agency happens to be a farmer-owned co-operative, then all profits are distributed annually to members.

Having concluded there is no systematic discounting of regulated vegetables, I must now consider the situation as it exists in respect of non-regulated products. The non-regulated vegetables for the fresh market are potatoes, mushrooms, tomatoes, cabbage, cauliflowers, onions, carrots, green and wax beans, celery, cucumbers, parsnips, spinach, asparagus, beets, peppers, sweet corn and rutabagas. The percentage share of the sales for each of these vegetables has been illustrated in Figure 3-B.

EVIDENCE CONCERNING NON-REGULATED VEGETABLES

In the Legislature and in the hearings conducted by the Resources Development Committee, there were allegations that fresh vegetables was one of the main areas of discounts being demanded by the retailers. However, even though the hearings were widely advertised and reported, very few vegetable producers contacted this Commission either to testify or to disclose information on a confidential basis in support of these allegations. In fact, most contacts with this farm community were initiated by Commission staff on my instruction.

1. ONTARIO FRUIT AND VEGETABLE GROWERS ASSOCIATION

Mr. Howard Staff, the President of the Ontario Fruit and Vegetables Growers Association, gave evidence at the Inquiry and submitted a brief on behalf of that organization. Although he was unable to testify as to having first-hand knowledge of discounting, his evidence was

helpful and for this reason, the substance of his testimony is set out extensively below.

The Ontario Fruit and Vegetables Growers Association represents the majority of fruit and vegetable growers in Ontario, approximately 14,000 in number. The directors are elected from the various fruit and vegetable marketing boards and from local organizations.

Mr. Staff estimated the total crop value produced by association members to be $250 million. Seventy-five million dollars of that produce is not regulated by marketing boards while $175 million is regulated.

The Association's brief indicated that, in 1978, Mr. Staff's predecessor in office had been informed of a discounting practice being used by Loblaws in payment for produce and that Dominion Stores were intending to instigate the same practice. The Association began to monitor the situation and make inquiries. As a result of their investigation, they reached the following conclusions:

(a) that all discounts were paid by shippers or packer-shippers and not producers; and

(b) that at no time had the minimum price level established by any marketing board been violated.

In the opinion of the Association, growers of produce not subject to marketing board regulation are more

vulnerable to discounting practices than are growers subject to regulation. The evidence received at the Inquiry supports these conclusions.

2. MR. WALTER SHEBEC

One individual grower who offered testimony to this Inquiry is Mr. Walter Shebec whose farm is located in the Waterford area. Mr. Shebec's farm consists of 80 acres on which he grows tomatoes, lettuce, cucumbers, cabbage, pumpkins and squash, for the fresh market. For the past twelve years he has been selling vegetables to the various chains.

Approximately two weeks before Mr. Shebec's crop is ready for delivery, he meets with the buyers of chains to see if they will buy his produce. At this meeting, the terms of purchase, including volume and price, are discussed.

One other term of purchase discussed is the amount to be discounted or deducted from the price established. In the past two or three years, these discounts have ranged from 5% to 15% of the gross value of his sales. Mr. Shebec introduced statements attached to his cheques for produce sold to The Oshawa Group in 1978. These statements indicated a deduction of 5% from the gross amount invoiced.

In 1978, Mr. Shebec met with the produce buyer at Loblaws for the first time. According to Mr. Shebec's testimony, the buyer wanted to buy tomatoes provided Mr. Shebec granted a 10% discount. This transaction was not

finalized though Mr. Shebec did sell dill cucumbers and peppers to Loblaws at no discount.

In 1977, Mr. Shebec met with the buyer from Dominion Stores who was interested in purchasing his tomatoes and a discount of 10% was discussed. This transaction was never finalized either, but in the same year, Mr. Shebec did supply cabbage to Dominion Stores for which he received a cheque with no explanation as to how it was calculated. He complained to the buyer who advised Mr. Shebec that if he did not approve, Dominion could obtain other suppliers.

In the result, Mr. Shebec thereafter sold most of his cabbage to M. Loeb Limited and to The Oshawa Group. The discount that Oshawa deducted from his cheque varied from 5% to 15%, according to Mr. Shebec's testimony. He complained about the 15% deduction with no success and continued to supply Oshawa for another two weeks on those terms.

The following year, Mr. Shebec refused to supply Oshawa unless they discontinued the 15% deduction. Oshawa buyers telephoned Mr. Shebec "on the average of three times a week" to ask him to supply their stores. Finally, an Oshawa buyer advised Mr. Shebec that Oshawa had decided to deduct only 5% if he would supply them with produce again. Mr. Shebec agreed to these terms.

In September or October of 1978, Mr. Shebec dealt with Knob Hill Farm buyers at the Food Terminal. According to the witness, Knob Hill usually quotes the lowest possible

price. Mr. Shebec alleged that if the transaction involves substantial volumes, Knob Hill "rounds off" the cheque. Rounding off may result in a reduction of the initially quoted price in the amount of 15% to 30%, according to Mr. Shebec's calculation.

Mr. Shebec estimated the amount of all discounts allowed by him to various retailers in 1978 to be four thousand dollars ($4,000) in total. He further testified that he has always been confused as to why he should allow discounts.

Upon examination by myself, the witness testified that he always knew the amount of the discount before delivery. He also indicated that, before delivering to a chain, he contacts the provincial representative at the Food Terminal in order to ascertain the daily market price for the product. He further testified that the price obtained for his product from the chains is a compromise figure, agreed upon by himself and the chain, between the daily market price and the figure offered by the chain.

Upon cross-examination by counsel for Dominion Stores, Mr. Shebec admitted to an advantage in selling to the chain compared to selling at the Food Terminal. In selling to the chains, a grower normally sells all his produce at the market value. On the other hand, a grower who sells on the open market is not guaranteed a sale and may eventually have to transport back home whatever produce he has left.

3. THE CHAIN STORES

Mr. Peter Allister Graham, Vice-President, testified on behalf of The Oshawa Group Limited in response to Mr. Shebec's testimony. The Oshawa Group is a Canadian company engaged primarily in the wholesale distribution of food products. In Ontario, this company supplies 137 IGA franchise stores and operates 61 company-owned units in addition to supplying many other retail outlets.

Mr. Graham testified that most fresh produce is bought centrally by his company, meaning, products are purchased from the Ontario Food Terminal, from packer/shippers or from other "pools" of products produced by different farmers. A small percentage only is transported directly from the farm to the local store. This witness further indicated that centrally purchased products are purchased on a discounted basis or, as he described it, on a "net basis."

In the case of produce delivered directly from the farm to the local store, the company usually pays Toronto price plus a delivery charge. The supplier is, in turn, charged a discount in return for the benefit of a guaranteed payment as opposed to the situation where the grower transports his product to the Food Terminal and is not assured of a sale. Mr. Graham thus maintained that a discount of 5% is reasonable compared to the risk of selling at the farmers' market or to the expense of paying 15% to a broker.

Mr. Graham then gave his version of his buyers' dealings with Mr. Shebec. Prior to 1977, The Oshawa Group had purchased fresh produce from him for a period of approximately eight years. Mr. Shebec tended to ask a premium price for his products. The discount was 5% during this period of time. In the fall of 1977, Mr. Shebec grew a patch of pumpkins which he attempted to sell on the cash market. He sold a quantity of the largest and best for a good price and then called the Oshawa buyers to see if they would purchase the unsold lot. At this point, Oshawa had a sufficient supply of pumpkins. They agreed to purchase Mr. Shebec's pumpkins because of their past dealings with him, however. A 15% discount was agreed to by Mr. Shebec, which yielded him a net price higher than the price received by other suppliers of pumpkins.

In the fall of 1977, Oshawa suggested to Mr. Shebec that the discount should go up to 15% on all products. He refused this suggestion. Nevertheless, Oshawa purchased 50% more produce from Mr. Shebec in the following year.

In defence of The Oshawa Group's dealings with Mr. Shebec, Mr. Graham testified it was the policy of his company to buy all produce as cheaply as possible so that it may be sold to the consumers at a low price.

Mr. Steve Stavro, President and owner of Knob Hill Farms, testified that his firm buys 75% of its produce directly from the farm. Only when a shortage occurs will Knob Hill buy produce from the Ontario Food Terminal. His

firm does not ask for a discount, but agrees with a producer on a net price or "bottom-line" figure.

With regard to Mr. Shebec's allegation that Knob Hill rounded off cheques, Mr. Stavro said this was done because the cabbage Mr. Shebec supplied was not of an appropriate size and weight. Knob Hill only purchased the cabbage because Mr. Shebec could not sell his product elsewhere.

Mr. Allen Jackson, President of Dominion Stores Limited, testified that his company negotiates on a bottom-line price with growers and does not ask for discounts. He was of the view that farmers are denying themselves benefits by not discounting. He further testified that a deduction was made from Mr. Shebec's cheque only because he was shipping in used containers. In fact, according to this witness, Mr. Shebec was overpaid for the produce he brought to market.

Mr. Jack Levine, President of Steinberg Incorporated, testified that the Ontario operation (Miracle Food Mart) of his company once discounted twenty of its suppliers of farm produce by the amount of 1%. Miracle discontinued the practice when asked to do so by the Ontario Food Council, a defunct agency of the Ontario Government.

Mr. David Nichol, President of Loblaws Limited, indicated that Loblaws had a 2% discount policy with producers of fruits and vegetables, a discount which has since been discontinued. He further testified that no product was bought illegally below marketing board minimum prices.

Mr. Kennedy, the President of the Great Atlantic and Pacific Company of Canada Limited (A & P), testified that this firm receives no discounts on fresh produce. His company prefers bottom-line bargaining.

D. FRUIT

Fruit represents only 1.1% of the value of farm products not subject to marketing board regulations. Many products in this category are sold directly to chains only in very small proportions: less than 1% of the sales of fresh apples, sour cherries, grapes, peaches, pears, plums, prunes and raspberries are sold directly.

Only three fresh fruits -- sweet cherries, strawberries and cantaloupes -- are sold in significant proportion to chain stores. About 50% of fresh sweet cherries, less than 30% of fresh strawberries, and less than 25% of fresh cantaloupes are sold directly to chains.

The markets for these fruits are characterized by the presence of many buyers. The majority of these fruits is marketed through pick-your-own or roadside outlets according to the Ministry of Food and Agriculture estimates provided to this Commission. Therefore, discounting, at least by the major chains, does not appear to be a serious problem in the sale of these commodities.

I will now consider the evidence given at the hearings in order to investigate this preliminary conclusion more closely.

1. MR. JAMES MCGUIGAN

Mr. James McGuigan is a farmer and a member of the Ontario Legislature who testified before the Commission. Mr. McGuigan's family has farmed for six generations. His farm consists of 200 acres; this acreage is mainly devoted to the growing of fruit: strawberries, cherries, raspberries, peaches, plums, pears and apples.

In the early 1950's, Mr. McGuigan started selling fruit to a Food City outlet in Chatham. At first, this outlet discounted the amount he claimed was owing by 3% but this amount gradually increased to 7%. Neither the discount nor the increase was negotiated. The witness was given no explanation for the deductions other than that the discount was a condition of doing business with this particular outlet. As a result, Mr. McGuigan discontinued selling to Food City and commenced selling to Loblaws and Dominion Stores which did not discount his cheques. At the present time, the witness is only selling to Dominion Stores a firm which his family has dealt with for over forty years. During that time, Dominion has never discounted his produce.

Mr. McGuigan also sold fruit to a Loeb's I.G.A. store in Wallaceburg. Prior to 1978, this outlet paid cash on delivery with no discount. In January of 1978, however, he delivered a shipment of apples to the Wallaceburg I.G.A. for which he received a cheque reduced by $14.16 from the amount invoiced to the store. This represented a discount

of 6%. A similar percentage discount was taken for his February, March, April and May deliveries of apples.

The son of the witness complained in April to Loeb's Accounts Payable Department and pointed out that such a discount was in contravention of the Apple Marketing Commission regulations. The son was told to add 6% to his invoices in May and June to accommodate this reduction. His son added 6% to invoices in accordance with Loeb's instructions. The McGuigan's account with the Wallaceburg I.G.A. was discontinued in September of 1978. The discontinuation occurred because of a new corporate policy instituted by the firm to the effect that fruit was to be delivered to company warehouses instead of directly to stores.

In his testimony, Mr. McGuigan was critical of the Apple Commission's agreement to allow retailers an 8% warehouse allowance. He was supported in this position by another apple grower who testified, namely, Mr. Al Ferri. Mr. McGuigan was of the opinion that the fruit would be better handled by apple growers than by warehouse handlers. He also criticized the warehouse system for the reason that certain types of apple -- including Ontario's best-known apple, the MacIntosh -- will not withstand the extra handling that a warehouse system creates. This witness did not deny the right of retailers to use the warehouse system but felt that the Apple Commission should have discouraged its institution for the above-mentioned reasons.

Mr. Gerry Long, the Chairman of the Apple Commission, also gave testimony on this point. The Apple Commission consists of representatives of the interests of consumers, retailers, processors, packers and growers, although the majority on the Commission consists of growers. The function of the Commission is to establish minimum prices and to promote the sale and consumption of apples.

In Mr. Long's view, the warehouse system is inevitable because of computerized technology. The Apple Commission's decision to allow an 8% warehouse allowance was the result of prolonged deliberation by the Commission and was arrived at by democratic process. Although some representatives wanted a higher rebate, Mr. Long expressed the opinion that 8% was a fair percentage when compared with the Apple Commissions of Quebec which allows a 12%, and of Nova Scotia which allows a 10%, warehouse allowance. Mr. Long also stated that the Ontario Commission is faced with competition from outside the province and must take this competition into account when making decisions affecting Ontario growers.

Mr. Frank Warnock, the President of M. Loeb Limited, testified on behalf of that company as to Mr. McGuigan's allegations. He testified that the I.G.A. store manager asked Mr. McGuigan's son for a discount on the apples as the store manager wished to buy as cheaply as possible. The son agreed to the discount in order to obtain the business of that store. Furthermore, the witness testified that the store manager's request for such a discount was against Loeb company policy. Although discounting is contrary to

company policy, it takes place "day after day in the field" as store managers attempt to obtain the lowest net price possible, he explained.

Mr. Warnock further testified that from September until November 1st, of each year, producers ask stores for less than Commission price because they are anxious to obtain the business. According to the witness's recollection, the Ontario Apple Marketing Commission at one time allowed a discount of six or seven percent.

2. THE 1978 STRAWBERRY CROP

Although not strictly within the terms of reference, a situation concerning the 1978 strawberry crop arose many times in the evidence. In 1978, many Ontario farmers were either unable to sell their strawberries to the retail chains or were obliged to sell at extraordinarily low prices to the retail chains. The chains were accused of creating this problem by importing American and Mexican strawberries during the Ontario growing season.

Examined in testimony on this accusation, the chains provided a more or less uniform explanation. In 1978, they had ordered strawberries from California and Mexico in advance of the normal Ontario season, and did not expect them to arrive at the time the Ontario crop ripened. Unfortunately, both the Ontario and Quebec strawberry crops ripened exceptionally early due to unusual weather conditions and came on the market at the same time as the imported crops arrived. Thus, several of the chains had to refuse to buy

the Ontario strawberries as they had already contracted for the imports.

It is my conclusion based on this evidence that the problem was caused by unfortunate circumstances, and not as the result of intentional action by the chains or other retailers.

GENERAL OBSERVATION ON REBATES IN FRESH PRODUCE

As previously stated, the evidence received in this Inquiry indicates that farm products not under marketing boards are more likely than farm products under marketing boards to be the subject of rebates, especially certain vegetables and fruits grown for the fresh market. These products represent approximately 4% of 1977 Ontario farm cash receipts. Although this percentage may seem insignificant, I realize that it can be a serious matter to the individual producer.

While some chains appear to have always purchased on a bottom-line basis, certain large chains have practiced discounting in respect of fresh produce at various times prior to 1978. Complaints as to such practices were received by the now defunct Ontario Food Council. Mr. Douglas Williams, former Chairman of the Food Council, testified as to investigations conducted by this agency during the period 1968 to 1978.

In 1972, the Food Council received complaints that Dominion Stores were asking for a 2% discount in return for

"fast" payment of accounts. Prompt payment is required by the regulations under The Farm Products Grades and Sales Act, (R.S.O. 1970, c. 161); the Council therefore was of the opinion that this could not be the reason for a discount. The Food Council contacted Dominion Stores to this effect, upon which the chain discontinued its practice.

In 1977, concern was expressed to the Food Council about a new purchasing policy of Dominion Stores requesting packer/suppliers of fresh meats to invoice individual stores at one-and-one-half cents per pound above the agreed price. This incident is recorded here because of its similarity to the incidents concerning fruits and vegatables. The meat packers were to remit the one-and-one-half cents overcharge at the end of each month. The Food Council verified these concerns with the Meat Packers Council, an organization representing the interest of packer/suppliers, and conveyed this organization's objections to the authorities at Dominion Stores. In the result, the company again agreed to discontinue its practice.

In 1978, producers complained to the Council that Dominion Stores and Loblaws were "strongly suggesting" to producers that they pay a 2% rebate on sales of fresh fruit and vegetables. The Food Council once again contacted the firms involved with the result that the practice was discontinued.

Representatives of certain chains gave evidence that they were strictly opposed to initiating rebates in respect of farm produce. Mr. Levine, President of Steinberg's,

testified that he was opposed to discounting sales of fresh produce and had instructed his buyers not to do so. Mr. Norman Fingler, Toronto Zone Manager of Canada Safeway Limited, stated that his firm has not received discounts from suppliers of fresh fruits and vegetables except from one supplier, a vegetable packer. This witness assumed that if the rebate was offered to his firm, it was being offered to the trade generally and on this condition, Safeway accepted the offer.

Representatives of chains that practiced discounting in the past testified to their view that rebates were earned by them. According to these witnesses, discounting usually permits a producer to sell his entire crop without running the risk of being left with surplus that, at best, must be disposed of in distant markets.

As to the present situation, it would appear that the discounting of fresh produce was discontinued in 1978 because of the publicity given to the practice in the Legislature and upon the formation of this Commission. During the week of October 1st, 1979, Robert Weist of Commission staff carried out ten interviews with persons associated with the fresh fruit and vegetable sector, including growers, presidents of various associations and shippers. As a result of these interviews, he submitted a memorandum introduced in evidence. This memorandum indicated that the major retailers did not ask growers for, or demand of them, any rebates during the 1979 growing season.

CONCLUSIONS

The following summarizes my conclusions on the evidence examined in this chapter:

1. Farm products are subject to complex and varied systems of sale in Ontario.

2. The sale of 40 farm products representing 57% of the 1977 total receipts for Ontario farm products is regulated by 23 marketing boards. Producers under marketing boards experience no rebating without the knowledge and consent of their boards.

3. The sale of farm products representing 43% of 1977 total receipts is not subject to marketing board regulation. There was no evidence of, nor did investigations indicate, any systematic rebating in respect of livestock and field crops except for one incident reported to the Ontario Food Council in 1977. The only evidence of rebating pertains to non-regulated fresh vegetables and fruit as summarized in the next paragraph.

4. From time to time prior to 1978, rebating has occurred in respect of fresh vegetables and fruit not regulated by marketing boards. The total sales of these products represent approximately 3.4% of the total receipts for Ontario farm

produce. In respect of these practices, I have reached the following conclusions:

(a) that the reasons for these rebates were not understood by the growers involved;

(b) that the rebates were not illegal but were the result of hard bargaining;

(c) that these practices were discontinued by 1979 as the result of the actions of the Ontario Food Council and the adverse publicity generated by the Resources Development Committee and this Royal Commission.

5. Certain producers of non-regulated fresh vegetables and fruits are in a very weak bargaining position. This is true of the producers of perishable products such as tomatoes, strawberries and cherries who must sell their produce within a short period of time or risk losing their investment.

RECOMMENDATION

1. It is unfair for a retailer to obtain non-negotiable rebates from producers of fresh vegetables and fruits whose products are perishable. Although systematic discounting does not appear to be practiced in respect of such commodities at the present time, it is my recommendation that the Legislature should provide for the creation of a "watchdog" mechanism to ensure that discounting

practices do not reappear. Such a solution is necessary because of the intense competition between retail chains in Ontario to buy as cheaply as possible.

CHAPTER 4

IMPORTS AND REBATES

GENERAL

The Ontario consumer is able to purchase food grown in all parts of the world from his local food retailers. There is a large demand for a great variety of food products for three main reasons. First, Ontario is an affluent society and has been able to pay the price for such products. For example, during the 1930's an orange was an unusual treat found only in the Christmas stocking; today, most consumers expect citrus juice for breakfast as a matter of course. Second, urban centres such as Toronto have received a large number of immigrants from all parts of the world. These ethnic groups have a preference for many foods of their native lands. Third, Ontario, because of its northern climate, is unable to produce certain products such as citrus fruits, cocoa, coffee, tea, and sugar. These must be imported.

It would be an almost impossible task for this Inquiry to investigate all the sources of imported foods, both from an economic and physical standpoint. Consequently, the Inquiry concentrated on imports from the United States which is the largest exporter of food to this province.

The conclusions reached in this chapter are based on evidence heard at the Inquiry and interviews with provincial and federal departments, food brokers and food retailers. In addition, I gained a great deal of information

from inquiries made in California, where Commission Counsel and I travelled for the purpose of interviewing growers, food exporters, wholesalers, retailers and state food inspectors.

SIZE OF ONTARIO AGRICULTURAL IMPORTS

In 1978, Ontario imported agricultural products worth $1,724,624,000 as analyzed in Table 4-A. This represents an amount equal to 56.8% of the value of Ontario farm cash receipts. Ontario accounts for 40.5% of Canadian agricultural imports. These figures are based on the value of goods that cleared Ontario ports and are not adjusted for further shipment of goods between provinces.

As the table indicates, the field crop category is the largest single commodity group of imports with sales amounting to $704,569,000. This group includes plantation crops such as coffee, tea and cocoa. This category is followed by the livestock and livestock products group ($325,232,000) and the fruits and nuts group ($322,451,000).

SOURCES OF ONTARIO AGRICULTURAL IMPORTS

Table 4-B shows that the United States is by far the largest source of Ontario agricultural imports, accounting for 62.6% of the total. Other countries which export important numbers of products to Ontario include the western European countries, Britain and the Caribbean countries.

TABLE 4-A

ONTARIO'S AGRICULTURAL AND FOOD IMPORTS BY COMMODITY GROUP

1978

	Value of Imports ($,000)	Percent of Total Imports
Livestock and livestock products	325,232	18.9
Field crops, including plantation crops such as coffee, tea and cocoa	704,569	40.9
Vegetables	155,821	9.0
Fruits and Nuts	322,451	18.7
Other	216,551	12.6
	1,724,624	100.1

SOURCE: Ontario Ministry of Agriculture and Food.

TABLE 4-B

SOURCES OF ONTARIO'S AGRICULTURAL AND FOOD IMPORTS

by Geographic Origin - 1978

Source	Value of Imports ($,000)	Percent of Total Imports
United States	1,079,568	62.6
European Economic Community excluding Great Britain	121,645	7.1
Great Britain	67,702	3.9
Caribbean	41,899	2.4
Japan	2,645	0.2
Other	411,165	23.8
	1,724,624	100.0

SOURCE: Ontario Ministry of Agriculture and Food.

THE MECHANICS OF BUYING IMPORTED AGRICULTURAL PRODUCTS

Ontario wholesalers and retailers buy imported agricultural products through three channels:

1. DEALERS

Dealers in Ontario sell at the various markets of agricultural products. For example, many sell fruits and vegetables at the Ontario Food Terminal, a large wholesale produce market located in Toronto. Dealers obtain their products either by buying directly from the foreign producer or his agent, or by buying through or from a Canadian or foreign broker. Dealers sell to wholesalers and to all types of retailers.

2. BROKERS

Canadian or foreign brokers operate by introducing buyers and sellers of imported products. Most brokers specialize in a small number of products, and generally do not take title to the goods. Many brokers are dealers and vice versa.

3. DIRECT BUYING

Wholesalers and retailers may also buy directly from foreign producers or their agents. The procedure is quite simple in that the connection is made directly between primary producer and final retailer without the intervention of middlemen.

Ontario food retailers make use of all three supply channels described above. The general pattern is that larger retailers buy products directly, whereas smaller retailers purchase through dealers or brokers.

REBATES AND IMPORTS

The Commission received evidence from representatives of Ontario companies engaged in importing produce. Mitchell Pacific Limited is a wholesaler of domestic and imported produce located in the Ontario Food Terminal which deals mainly through food brokers when purchasing from United States. Both major chain retailers and smaller retailers purchase from Mitchell Pacific though the larger chains usually purchase from the company only where an unexpected demand for, or an unexpected shortage in, their own stocks occurs.

Mrs. Wyne Ciceri, the office manager of Mitchell Pacific, testified that the chains are desirable customers as they will take the majority of produce brought in on any given load imported. There is no written contract between packer/shipper, wholesaler or retailer as orders are placed by telephone. Much confidence is placed by each of the parties in these verbal agreements; as Mrs. Ciceri expressed it, "your word is your bond."

She further testified that Mitchell Pacific neither receives rebates from suppliers nor gives them on sales to retailers. She indicated that the trend is, in fact, towards better relations with the chains than was

historically the case due mainly to the fact that the older buyers, who were harder bargainers, have now gone. The chains are now willing to pay the price her firm invoices.

Commission Counsel and I visited representatives of two farmer/shipper operations located in the San Joaquin Valley of California. These operations sell a wide variety of fruits and vegetables to large and small chains in Ontario. The individuals we interviewed were most co-operative and answered our questions without hesitation. Both operations are very large compared to Ontario operations, each operation occupying 40,000 acres of land. These firms not only grow but grade and store their produce which they market throughout North America and other parts of the world. It was our impression that most of the farm produce in this valley is grown and marketed on a similarly large scale.

The representatives of these operations advised us that they receive inquiries daily from Ontario as to the prices of their produce. It is their practice to quote to all buyers from the United States or Canada a daily published market price, excluding freight from California. There is no deviation in price to accommodate larger volume orders though two prices are usually quoted. For example, a full carload of cauliflower may be quoted at $4.75 per hundred weight; any quantity less than a full carload may be quoted at a higher price of $5.25 per hundred weight. The difference in the two prices quoted represents the savings due to economies realized on loading and shipping full carloads as opposed to loading and shipping smaller

quantities bound for different destinations. The price differential must be related to actual savings in costs according to the Robinson-Patman Act of the United States, legislation which will be discussed more fully in Chapter 16.

CONCLUSIONS

The following summarizes my conclusions on the evidence examined in this chapter:

1. Generally, imported agricultural products are not subject to rebates in Ontario. Imported products are usually bought on a net price basis.

2. The pricing structure applying to imports from the United States, Canada's largest trading partner, is strongly influenced if not controlled by legislation in that country pertaining to discounting. Because of this legislation and because of the international competitive structure, there is little likelihood of rebates becoming an important factor in the price determination of agricultural products imported into Ontario.

CHAPTER 5

PROCESSOR/MANUFACTURERS AND REBATES

GENERAL

Briefly stated, the terms of reference require that I report on the effect of rebating practices on the farmer and the consumer. While the terms of reference strictly construed do not require me to inquire into the processor/-manufacturer level of the food chain, it is my view that the Inquiry would be incomplete if I failed to do so. This is particularly so because this level is the principal source of rebates in the food industry.

In Chapter 2, I have catalogued and described in detail the various types of rebates, approximately twenty in number. These were categorized into five main groups:

A. Economies of Scale

B. Advertising

C. Service

D. Finance

E. Miscellaneous

As expressed in Chapter 2, processor/manufacturers (to be called "processors" or "manufacturers" hereafter) offer rebates to retailers and wholesalers in order to promote the sale of their products. Processors also achieve benefits from rebates due to volume sales, retailer advertising, special displays and reduced prices.

In the past few years, there has been a large increase in the number of products offered by processors. Processors offer rebates to retailers in order to promote their products in the face of stiff competition. Retailers recognize the benefits they can provide to a processor and consequently, they have developed "package promotions" that they offer to suppliers. Thus, processors are offering many kinds of rebates to retailers in order to sell their products while, at the same time, retailers are offering "promotional packages" to the suppliers.

In this chapter, I will not deal with the listing and delisting of products by retailers. This topic will be considered in Chapter 15.

EVIDENCE CRITICAL OF DISCOUNTING PRACTICES

The Grocery Products Manufacturers of Canada (G.P.M.C.) filed a brief on behalf of its members criticizing discounting practices as they presently exist in Ontario. The G.P.M.C. is a voluntary association of 93 companies engaged in the manufacture of grocery products, including food and non-alcoholic beverages in Canada.

The following paragraph from page 12 of the G.P.M.C. brief, gives a general idea of the G.P.M.C.'s concerns:

> "Each of the different rebates, discounts and allowances has a rationale which makes sense on its face. Where the allowance in amount and purpose relates in a direct way to the rationale, no special problems or

concerns are likely to arise from the standpoint of the public interest, the farmer, the consumer, or the manufacturer. However, where they, or the methods employed by the retailer to achieve them, depart from that rationale, concern may arise which warrants investigation."

The G.P.M.C. raises more particular areas of concern worthy of note at this point. First, they allege that if it were not for the extraordinary power of the retail buyer, processors would not necessarily choose to promote their products in the particular way required by the retailers; in other words, processors would spend their money differently if they felt free to spend it differently.

Second, they allege that a processor's negative response to a retailer's request for promotional money could adversely affect that processor's dealings with the retailer in the future.

Third, they allege that it is not uncommon for a retail buyer to suggest that the supplier raise his list price to accommodate an increased rebate.

Fourth, they allege that suppliers may interpret negotiations as more than "tough bargaining"; in fact, they interpret them as coercion.

Another witness who criticized present discounting practices was Mr. Ken Gadd, General Manager of the Canadian

Federation of Retail Grocers (C.F.R.G.). C.F.R.G. is a voluntary organization of independent grocers.

It was Mr. Gadd's view that co-operative advertising allowances are "exacted" (in other words, "demanded") by large retailers, rather than freely offered by suppliers.

Mr. Gadd's remarks were supported by the testimony of Mr. Art Ruttan, owner of Ruttan Foods Limited, a supplier of sugar substitutes. Mr. Ruttan characterized discounting negotiations as "extortion" on the part of the chains, though he later admitted that this word was perhaps too strong.

Mr. Archie McLaine, Vice-President of Marketing for McCain Foods Limited, was another supplier critical of some discounting practices. In particular, he objected to suppliers' offering money in the form of annual volume rebates. In his opinion, this money would be better spent on suppliers' own advertising, but he testified that this would be "difficult, if not impossible to negotiate."

EVIDENCE SUPPORTIVE OF REBATING PRACTICES

Not all processors were critical of discounting practices. Mr. Robert Bras, President of Menu Foods, a supplier of pet food, testified that retailers do not delist processors for failure to offer rebates. He also contradicted the theory that retailers take advantage of superior market power in discounting negotiations, pointing out that concentration at the manufacturing level is much

greater than it is at the retailing level due to the brand and marketing leadership of the manufacturers.

Mr. Peter McLinden, Vice-President and General Manager of Gay-Lea Foods Co-operative Limited, a co-operative formed by milk producers to process and market milk products, testified that he does not find the bargaining process to be harsh and oppressive. The pressure to lower prices comes from competitive sellers, not buyers, in his view.

Other processors gave evidence supportive of discounting practices as well, including members of the Grocery Products Manufacturers of Canada.

Mr. Douglas Mackie, Vice-President of the Borden Company, testified that his company makes its presentation to the retailer and the buyer either accepts or rejects the offer. Generally, Borden's will not negotiate modifications. Borden's is a member of the G.P.M.C.

Mr. John D. Herrick, Chairman of the Board of General Mills, testified that costs of rebate programs are increasing, mainly due to competitive pressure from other processors. It was his view that bargaining is a "hardnose business" for both parties. General Mills is a member of G.P.M.C.

Mr. Gary Culbert, Director of Marketing for Canadian Canners Ltd., testified that the firm annually sets its rebates to meet a specific target. His firm does not

negotiate rebates with any retailer. Canadian Canners is a member of the G.P.M.C.

Mr. Maurice O'Flynn, Vice-President of Sales and Marketing for Green Giant of Canada Limited, testified that his company's rebate program is non-negotiable as far as price and volume rebates are concerned, though short-term allowances are negotiable in response to immediate pressure from competitive processors. Green Giant is a member of the G.P.M.C.

Mr. Murray McEwan, President of Redpath Sugars Limited, testified that there is little pressure from retailers as to rebate levels. Most pressure results from a competitor's making a better offer to a retailer. Redpath is a member of G.P.M.C.

Mr. Jean M. Dubuc, National Sales Manager of Catelli Foods Limited, testified that his firm annually establishes a rebate program offered to all customers. To his knowledge, no retailer has ever attempted to change the program. He does not believe negotiation is coercive and feels his firm receives good value from co-operative advertising programs and volume rebates. Catelli is a member of the G.P.M.C.

This sort of evidence was given not only by processors but by suppliers at other levels of the food chain as well.

Mr. Moe Cohen, President of Dominion Farm Produce, a packer of farm products operating in the Bradford area,

testified that his firm initiated a volume rebate program which yielded results satisfactory to the firm. I have already referred in Chapter 4 to the testimony of Mrs. Ciceri of Mitchell Pacific Ltd., a fruit and vegetable wholesaler at the Ontario Food Terminal in Toronto. As stated previously, Mrs. Ciceri is not critical of bargaining with retailers. In fact, she expressed the view that over the last few years, "bargaining is a lot easier" compared to previous years.

Mr. Ken Harwood is a partner in J&K Farms which grows ten to twelve thousand pumpkins a year. This firm sells approximately half its crop to A&P. He testified that J&K Farms has always been treated fairly by A&P. No discounts are asked for by the retailer.

In the previous paragraphs, I have paraphrased the evidence of processors, wholesalers and producers relating to discounting practices. I will now deal with the evidence tendered by retailers.

Mr. Alisdair McKichan and Mr. J.P. Carter, President and Vice-President respectively, submitted a brief and gave evidence on behalf of the Retail Council of Canada. The Council is a voluntary association of retailers in Canada. Their members perform over 65% of Canada's total retail store business. In the Ontario food industry, it represents directly the interests of the large chains and indirectly the interests of independent merchants affiliated with wholesale and franchise corporations.

Mr. Carter testified that the degree of concentration in grocery-retailing sectors is considerably less than in many grocery-manufacturing sectors.

The Retail Council brief denies allegations that retailers impose package promotions on the processors; to quote the brief:

> "The reality is different. Retailers prepare schedules outlining their individual product promotional capabilities....Contrary to the impressions that may have been created, it is suppliers who are responsible for inducing pressure for the establishment of particular allowances or discounts.
>
> "Discounts and allowances are by no means unique in the food sector of retailing. Every trade has its own range of discounts, allowances or promotionally sponsored plans which meet the needs of both buyers and sellers."

Mr. Jack Levine, President of Steinberg's, testified that though his firm is sometimes able to negotiate with a supplier resulting in rebate level increases, Steinberg's does not have a policy which dictates that a supplier should raise his price to accommodate discounts. He added that flexibility in negotiations does not depend on the size of the supplier; small suppliers can be just as inflexible as large suppliers. In fact, his company

prefers to keep the small independent entrepreneur in business in order to balance the market power of the large supplier.

The brief of A&P Canada Ltd., presented by the President of the company, Mr. Edward Charles Kennedy, categorically denies that A&P has ever exacted a rebate from any of its suppliers or potential suppliers. A&P requires a supplier to warrant in writing that the discounts and allowances offered are being offered to all purchasers of like quality and quantity. One reason that a warranty is required, according to the testimony of the witness, is to ensure that A&P is getting the same rebate as other retailers.

Messrs. Robert Glyn Spelliscy and Norman Donald Fingler testified on behalf of Canada Safeway Ltd. They testified that the only reason Safeway participates in rebate programs is because suppliers offer these programs. Safeway does not bargain with anybody. Furthermore, it is Safeway's company policy not to suggest that a supplier build in a rebate before quoting a price.

Mr. David Nichol, President of Loblaws Ltd., testified on behalf of this company. The witness stated under oath that Loblaws does not pressure suppliers for rebates; the pressure for large rebates, in Mr. Nichol's opinion, comes from other suppliers. He indicated that the large suppliers can be very independent. Mr. Nichol testified that the president of Proctor and Gamble, for example, has never contacted him about business, but that Loblaws

nevertheless carries certain Proctor and Gamble products because of consumer demand. Asked whether Loblaws demands from suppliers that they raise their prices in order to accommodate a discount, Mr. Nichol stated that his firm is only concerned with the net price.

Messrs. Thomas G. Bolton and Allen C. Jackson testified on behalf of Dominion Stores Ltd. Dominion is offered cost reductions by suppliers who expect Dominion to earn these reductions, Mr. Bolton stated. The nature of the service to be performed may be stipulated unilaterally by the supplier, as in the case of cash and volume discounts, or negotiated, as in the case of promotional allowances.

With regard to allegations that bargaining is coercive, Mr. Jackson testified that his firm instructs its buyers to be firm but fair with suppliers:

> "It's our job to buy at the lowest possible price. We are the consumer's agent, we are the balance of power between the consumer and the producer or manufacturer. As far as I am concerned, if there is any...coercion, and it is brought to my attention, it is investigated."

PRELIMINARY CONCLUSIONS

As indicated above, there are contrary views as to the nature of the bargaining for discounts. Is it coercive or is it merely hard bargaining?

The bulk of the evidence supports the view that it is "hard bargaining". Retailers and wholesalers endeavour to buy as cheaply as they can from the supplier, so as to sell as cheaply as they can to the consumer. The competition for consumers is intense.

At the same time, processors are anxious to sell their products and the competition is keen to get on the shelves of the retailers and wholesalers. They offer various rebates and other "deals" to reach this goal.

SURVEY OF ONTARIO FOOD PROCESSORS/MANUFACTURERS

The above conclusion is supported by the results of the survey performed by the Commission's consultants who surveyed 123 food processors in Ontario by written questionnaire, which is reprinted as Appendix 4. The consultants received 87 usable returns for analysis from firms engaged in the food processing industry of various products, throughout Ontario. The purpose of this survey was to obtain the data necessary to analyze the financial performance of the processors and the effects of rebates on this performance.

The data collected from processors indicated sales, in the most recent fiscal year, ranging from a minimum of $118,000 to more than $1 billion. The average sales volume was $115.6 million. Procesors are categorized by sales volume in Table 5-A. The sales volume of firms is used as a measure of size throughout this Report because market power, especially in relation to rebating and related

TABLE 5-A

BREAKDOWN OF PROCESSORS BY SALES VOLUME

Sales Volume	Number in Sample	Average Sales
Under $10 million	25	$3.8 million
$10 - $100 million	37	$53.5 million
Over $100 million	25	$319.4 million
TOTAL	87	$115.6 million

NOTE: 1. This figure includes non-food sales for certain companies.

2. All off-invoice allowances are included in these figures.

SOURCE: Processor/manufacturer questionnaire.

pricing practices, is more closely associated with sales volume than with any other measure of size.

Of the 87 firms filing usable returns, 85 firms produced name brand products, and 55 produced house brand products. The processors of name brands produced an average of 35 different name brand products. The processors of house brands averaged twelve different house brand products. Sales of name brand products averaged 86% of total food sales for all firms in the sample. For the smaller firms, with less than $10 million total sales, name brand sales averaged 71% of food sales. For the larger firms, name brand sales represented approximately 92% of food sales. See Figure 5-A.

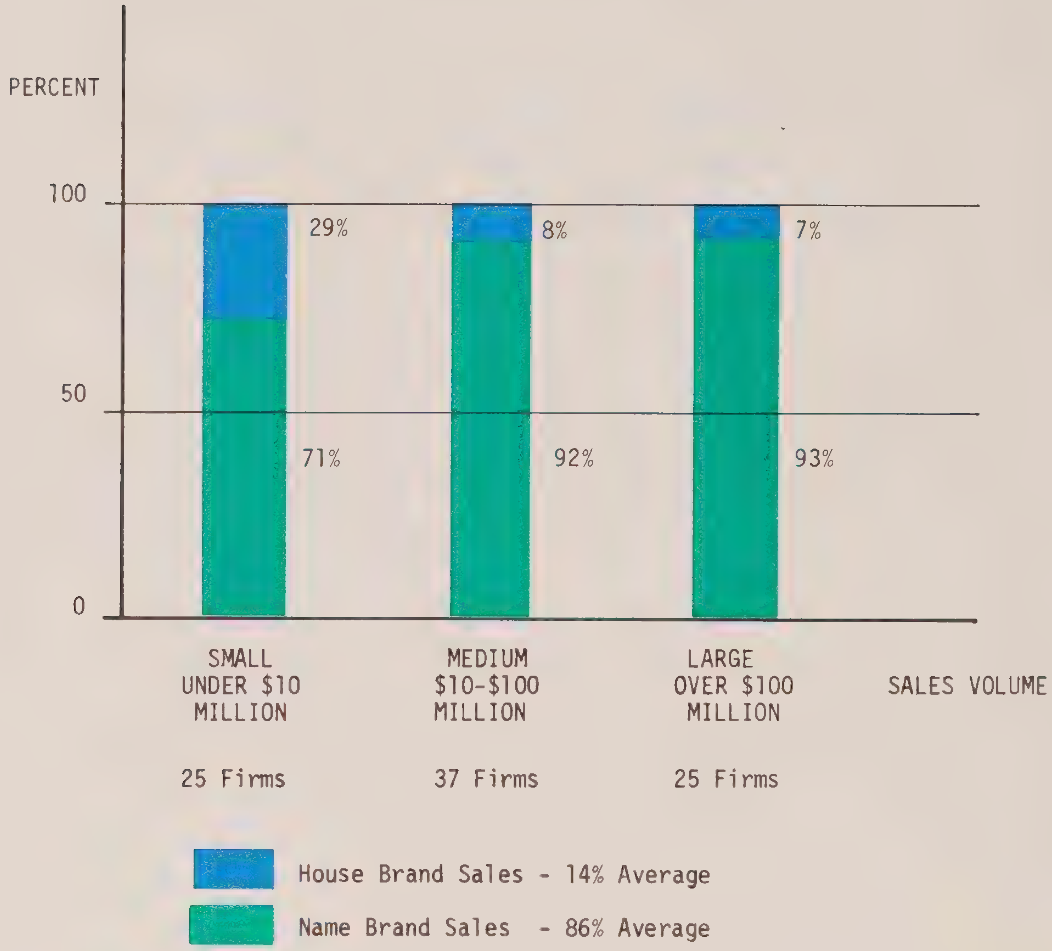
Financial data reported by the firms surveyed related in most cases to the food processing activities of the firm. In a small minority of cases, the consultants were unable to isolate the financial characteristics for food processing only. Tables 5-B and 5-C and Figure 5-B summarize the financial statistics for the firms in the sample.

The terms used in these tables and in this figure should be explained. "Gross margins" are calculated as the ratio of sales less the cost of goods sold to sales. "Cost of goods sold" represents the direct costs and raw material costs. "Net margins" are the ratio of net profits to sales. "Return on equity" is the ratio of net profit to the value of the shareholders equity.

FIGURE 5-A

PERCENTAGE OF SALES OF NAME AND HOUSE BRAND PRODUCTS

FOR 87 FOOD MANUFACTURERS



SOURCE: Processor/Manufacturer Questionnaire

TABLE 5-B

SUMMARY OF PROCESSOR FINANCIAL STATISTICS

Latest Period
(Fiscal Year Ends During 1977)

Sales Volume	Gross Margin	Net Margin (after tax)	Return on Equity (after tax)
Under $10 million	16.4%	-0.9%	-1.6%
$10 - $100 million	27.4%	2.6%	11.3%
Over $100 million	23.7%	3.1%	12.8%
Average	22.8%	1.8%	9.0%
Significant difference at 95% confidence level	Yes	Yes	Yes

NOTE: 1. A "yes" in the row labelled "Significant difference at 95% confidence level" means that one can say with 95% certainty that the figures in question, which are from our sample, represent populations in the real world that are actually different from each other. Conversely, one can say that there is less than 5% chance that, while reported figures are different, the figures for the entire population are the same.

2. All off-invoice allowances are included in these figures.

SOURCE: Processor/manufacturer questionnaire.

TABLE 5-C

SUMMARY OF FINANCIAL STATISTICS

Latest Three Period Average
(Fiscal Year Ends during 1977)

Sales Volume	Gross Margin	Net Margin (after tax)	Return on Equity (after tax)
Under $10 million	20.4%	-0.2%	4.5%
$10 - $100 million	27.8%	3.1%	13.3%
Over $100 million	23.3%	3.2%	12.8%
Average	24.2%	2.2%	11.3%
Significant difference at 95% confidence level	No	Yes	Yes

Anti-Inflation Board Food Processing Industry Sample

	Net Margin (after 50% tax rate)
1975	1.75%
1976	1.80%
1977	1.70%

Statistics Canada Food and Beverage Industry Data

	Return on Equity (after 50% tax rate)
1975	10.80%
1976	9.55%
1977	10.45%

NOTE: 1. All off-invoice allowances are included in these figures.

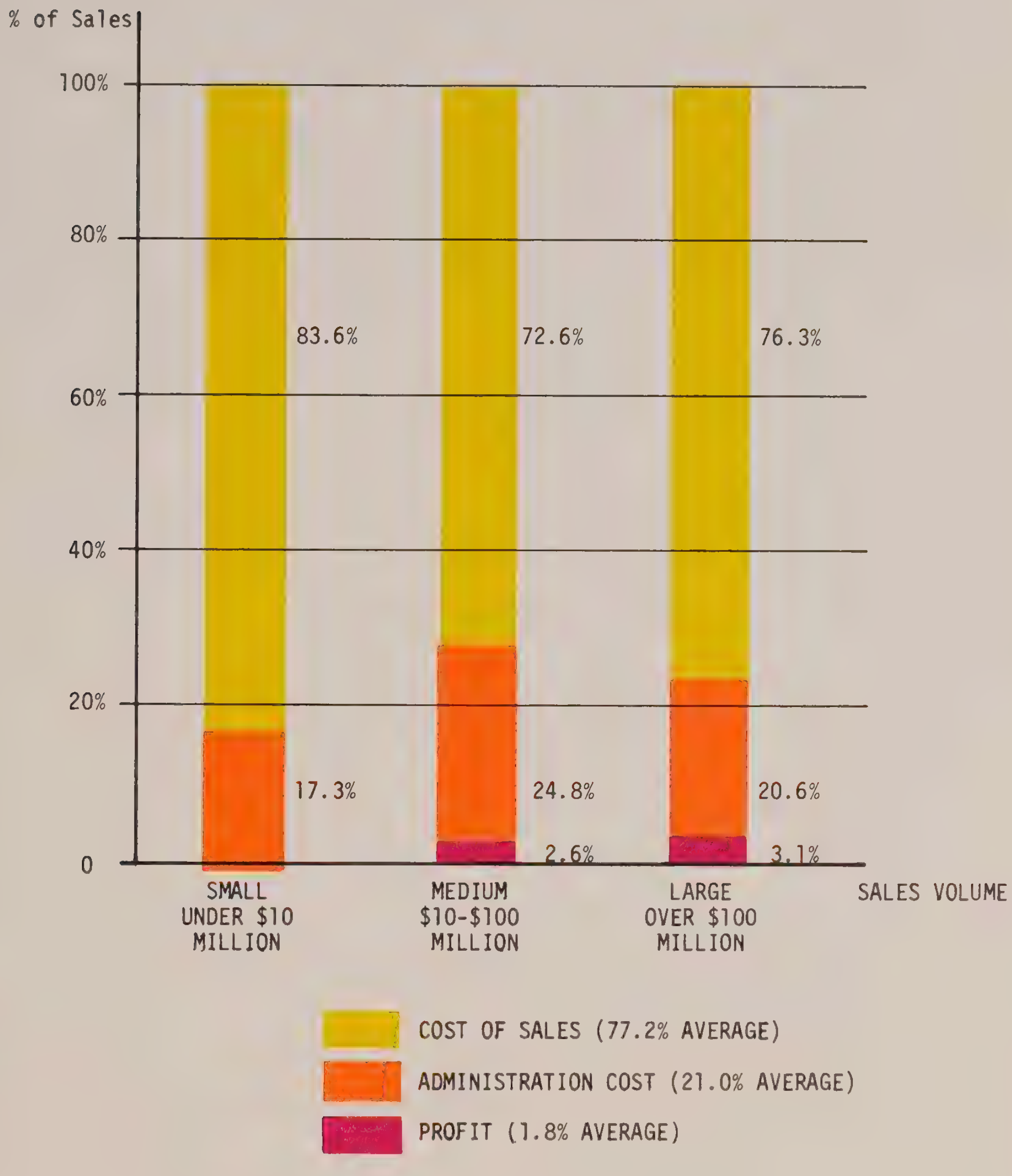
SOURCES: Processor/manufacturer questionnaire; Anti-Inflation Board, A Study of Profit Margins in the Food Industry (Ottawa, 1978), p.27; Statistics Canada, Catalogue #61-003.

FIGURE 5-B

COMPARISON OF AVERAGE OPERATING RESULTS

FOR 37 FOOD MANUFACTURERS

(FISCAL YEAR CLOSEST TO JANUARY 1, 1979)



SOURCE: Processor/Manufacturer Questionnaire

The financial characteristics of food processors perhaps can be most clearly summarized in point form as follows:

1. Gross margins for the smaller firms deteriorated during the last year. Gross margins, averaged over the last three years, were not significantly different for different sizes of firms.

2. There were significant differences in net margins compared with the sales volume of the firm for the latest fiscal year and the three-year period average.

3. Return on equity also varied significantly compared with the size of the firm. Thus, shareholders in smaller firms earned less than shareholders in larger firms. The position of smaller firms has deteriorated during the last three years.

4. Direct production and material costs are relatively constant for the larger processors, but are deteriorating for the smaller processors.

5. The financial risk for shareholders in smaller food processing firms is greater than in larger processing firms.

It was of some comfort to learn that the aggregated financial data reported by our consultants are comparable to the data reported by the Anti-Inflation Board in "A

Study of Profit Margins in the Food Industry."* The net margins in the A.I.B. food-processing sample across Canada are shown in Table 5-C. This table also indicates rates of return on equity for firms in the food and beverage industry provided by Statistics Canada.†

Given this financial background, I now turn to the question of discounts, rebates and allowances offered by processors. Processors surveyed reported the type and volume of rebates for their ten leading name and house brand products. The ten leading products accounted for 85.7% of total name brand sales, and 93.3% of total house brand sales.

A summary of rebate levels is presented in Table 5-D. The over-all level of rebates is equal to 10% of the processors' sales. Name brands carry a rebate of 10.6% while house brands carry 4.3%. The difference in rebate levels between name and house brand products was statistically significant at the 95% confidence level according to standard statistical measures.

The statistical term "significant difference at the 95% confidence level" allows for the fact that the figures treated are from a sample of processors and not the entire population of processors. The term means that one can say with 95% certainty that, where the averages in the sample (10.6% and 4.3%) are different, the averages in the entire processor population are actually different. Conversely,

* Catalogue No. 61-003 (Ottawa: 1978), p. 27.
† ibid., p. 23.

TABLE 5-D

SUMMARY OF REBATES OFFERED BY PROCESSORS

Sales Volume	On Name Brands	On House Brands	On All Brands
All Processors			
Under $10 million	8.0%	3.2%	7.5%
$10 - $100 million	12.4%	5.2%	12.0%
Over $100 million	10.2%	4.0%	9.6%
Average	10.6%	4.3%	10.0%
Significant difference at 95% confidence level	Yes	No	Yes
EXCLUDING MILK PROCESSORS			
Under $10 million	8.0%	3.2%	7.5%
$10 - $100 million	11.6%	4.3%	11.2%
Over $100 million	9.7%	2.6%	9.0%
Average	10.0%	3.5%	9.5%
Significant difference at 95% confidence level	No	No	No

NOTE: 1. The percentages of rebates on all brands are calculated as a weighted average by sales for name and house brand products.

2. All off-invoice allowances are included in these figures.

SOURCE: Processor/manufacturer questionnaire.

one can say that there is a 5% chance or less that, where the sample figures show different averages, the population actually shows identical averages. In brief, the measure of significant difference limits the conclusions one can draw from any sample when commenting on the entire population. Unless specified otherwise, the confidence level applied throughout this Report is the 95% confidence level.

Furthermore, the rebate levels for name brand products and the averages for all products varied significantly with the size of the firm. Medium-sized firms offer the highest levels of rebates on name and house brand products. One reason for this is that companies processing milk are over-represented in the medium-sized category; milk products carry an extremely high rebate level compared to other products.

The presence of milk processors in the medium-sized category raises considerably the average rebate level for this category. The consultants reported, upon analyzing the data excluding milk processors, that there was no significant difference in rebate levels between the different size categories. Milk processors are dealt with separately in the next chapter.

A summary of the average rebate levels for each of the various groups of rebates is shown in Table 5-E and Figure 5-C. This table and figure indicate that: first, rebate levels in the service and finance types of rebates varied significantly with the size of the firm; and second,

TABLE 5-E

SUMMARY OF REBATE LEVELS BY GROUP

Sales Volume	Economies Of Scale	Advertising	Service	Finance	Miscellaneous, Unspecified	Total
Under $10 million	1.3%	3.9%	0.8%	1.4%	0.1%	7.5%
$10 - $100 million	2.8%	5.1%	0.4%	0.8%	2.9%	12.0%
Over $100 million	2.0%	5.4%	0.1%	1.0%	1.1%	9.6%
Average	2.1%	4.8%	0.4%	1.0%	1.7%	10.0%
Significant difference at 95% confidence level	No	No	Yes	Yes	---	Yes

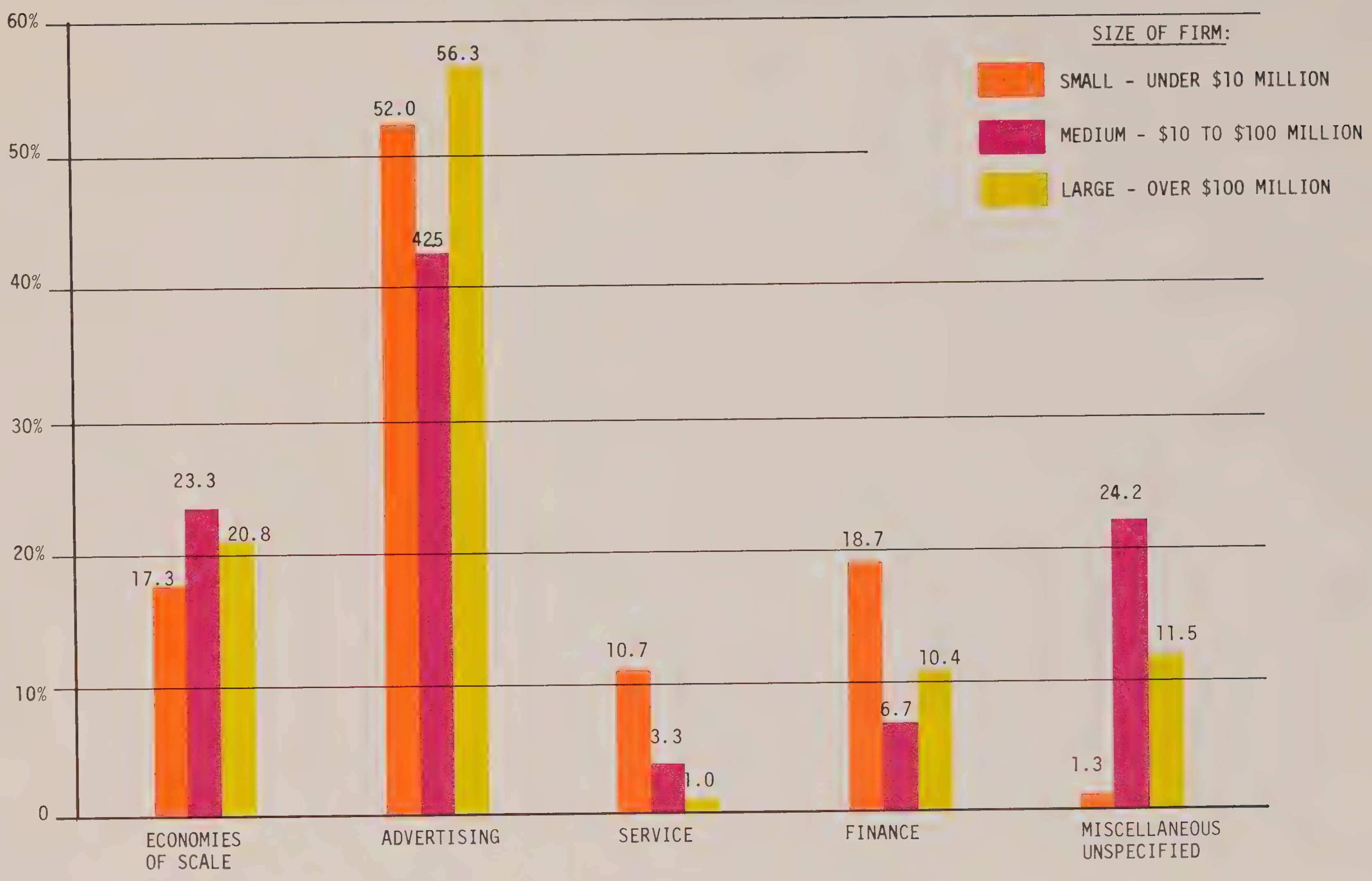
NOTE:

1. The figures are interpreted as the average rebate level offered on both name and house brand products for that group.
2. The figures represent rebates expressed as a percentage of processor sales, as reported in processor returns.
3. The unspecified rebates are those for which the processor could not specify the type but knew the total dollar value of all rebates offered.
4. Figures included all off-invoice allowances.

SOURCE: Processor/manufacturer questionnaire.

FIGURE 5-C

RELATIVE IMPORTANCE OF REBATE GROUPS



SOURCE: Processor/Manufacturer Questionnaire

smaller firms offer more service and finance types of rebates to their customers than the larger firms offer.

It is the consultants' view that these findings are due to the fact the smaller processors have limited facilities for storage and distribution of their products. The higher use of finance rebates could also indicate cash-flow problems encountered by smaller processors. The consultants found that many small canners, for instance, offer an early booking allowance for financial reasons and for production planning reasons. Before leaving Figure 5-C, it should be noted that the advertising rebate is the group of rebates most often used by all sizes of firms.

The consultants analyzed rebate payments by ownership. The processing companies that had majority control by a food retailer, either directly or through intermediate companies, were analysed in comparison to all other companies. It is the consultants' conclusion that there is no significant difference in rebate levels paid by the two groups of companies.

Considering the submission and the testimony of the consultants, and the cross-examination upon the same by all counsel to the proceedings, I accept the findings of the consultants in this and other matters.

ANALYSIS OF FINANCIAL PERFORMANCE

Having analyzed the financial performance separately and rebates separately, the Inquiry consultants carried out

an analysis to determine the effect of rebates on financial performance. This type of analysis requires expertise in economics and accounting, expertise that the consultants' project team possesses to a high degree. I adopt their analysis and quote it extensively in the following paragraphs:

"The objective of this analysis is to analyze the factors affecting financial performance across the food processing industry. There are 3 categories of factors affecting the financial performance of firms in an industry - uncontrollable, controllable and semi-controllable.

"The uncontrollable factors include such things as the level and growth of GNP, inflation, interest rates and unemployment. The firm cannot influence these factors through its operations. The firm's financial performance depends to some extent on the level of these factors.

"The controllable factors are those by which the firm operates. The firm's decision on these factors will relate directly to its financial performance in a given period of time. These controllable factors include decisions over output, production methods, investment plans, personnel, politics, and other aspects of business.

"The semi-controllable factors are those which the firm can influence through its decision

making process. However, the firm must also respond to competitive market pressures over which it has a varying amount of control. Some firms can control or dominate the market, others are in turn controlled by the market. Examples of these semi-controllable factors include the market structure, corporate concentration, prices, and for the purposes of this study, the nature of discounts, allowances and rebates.

"We [the consultants] used a multiple regression model* of the food processing industry to:

- Determine the key factors affecting financial performance.

- Quantify explicitly the relationships between these factors and the resulting financial performance.

"The measure of financial performance that we used was the return on equity for the most recent financial period. This measure best indicates the financial risk and return to investment in the food processing industry.

"We will try to explain the variation in financial performance by the semi-controllable

* A multiple regression model is a statistical method used to measure correlations between different factors; here, the factors are financial performance, rebates and sales.

factors. We identified our model by asking the following questions:

- How does the industry structure affect the financial performance of firms?

- What effect do discounts, rebates and allowances have on the financial performance of firms?

"We defined industry structure by the relative size of the firm. This measure is represented by the firm's overall sales volume. This sales volume will reflect the relative market power of the firm, even though it includes sales for activities other than food processing.

"The effect of discounts, rebates and allowances on financial performance is the main focus of this section. The use of rebates can affect the food processors as follows. Firms can offer rebates to such an extent that they offer a lower net price and thus become more competitive. Economic theory suggests that because these firms offer lower prices, their output should increase, and they should experience production economies of scale. These firms will continue to offer rebates until the marginal net revenue gained from the last unit of output equals the marginal cost of production and distribution. In other words,

these firms will offer more rebates as long as there is a contribution to the firm's profit.

"The model that follows will test this theory. The remainder of this section discusses the statistics of the regression analysis. The reader who is unfamiliar with statistics is referred to the final paragraph for a summary of the results. [Table 5-F presents the results of regression analysis on the processor sample.]

"We found the following regression equation using statistics for the latest financial period:

$$Y = -0.326 + 0.084\ X_1 + 0.326\ X_2$$

where: Y is percent return on equity

X_1 is the logarithm of sales (in thousands)

X_2 is the percent rebate level*

"What do these results mean? First, we should note that this model does not explain all the variations in return on equity. Sales and rebate levels only explain about 21% of the variation. Second, we should note that rebate levels are not a significant factor in explaining the variation in return on equity. The return on equity is not correlated with rebate levels. By including it

* The following are the regression statistics:
$R^2 = 0.206$
Adjusted $R^2 = 0.184$
Standard error of X_1 coefficient = 0.023
Standard error of X_2 coefficient = 0.355

TABLE 5-F

REGRESSION ANALYSIS OF PROCESSORS

REGRESSION I

$Y = -0.326 + 0.084\ X_1 + 0.326\ X_2$

where: Y is percent return on equity
X_1 is the logarithm of sales (in thousands)
X_2 is the percent rebate level

The following are the regression statistics:
$R^2 = 0.206$
Adjusted $R^2 = 0.184$
Standard error of X_1 coefficient = 0.023
Standard error of X_2 coefficient = 0.355

REGRESSION II

$Y = -0.326 + 0.091\ X_1$

Y and X_1 are percent return on equity and the logarithm of sales (in thousands)

The following are the regression statistics:
$R^2 = 0.197$
Adjusted $R^2 = 0.185$
Standard error of X_1 coefficient = 0.022

REGRESSION III

$X_2 = -0.001 + .022\ X_1$

where: X_1 is the logarithm of sales (in thousands)
X_2 is the percent rebate level

The following are the regression statistics:
$R^2 = 0.112$
Adjusted $R^2 = 0.099$
Standard error of X_1 coefficient = 0.007

NOTE: Includes off-invoice allowances.

SOURCE: Processor/manufacturer questionnaire.

in the model, we do not improve our ability to predict return on equity.

"We found that rebate levels were correlated with sales volume. That is, high sales volumes were associated with high rebate levels. We then dropped the variable for rebate levels from the model and found the following equation:

$$Y = -0.326 + 0.091\ X_1$$

Y is percent return on equity

X_1 is the logarithm of sales (in thousands)*

From this model we can say that industry structure as measured by sales volumes is important in explaining the variation in financial performance. An increase (or decrease) of 10% in a firm's sales will result in an increase (or decrease) of 0.9% return on equity.

"The relationship between financial performance and rebate levels is an indirect one...[R]ebate levels vary directly with sales volume. A more precise measure of the relationship between rebate levels and sales is obtained through a regression equation. We found the following equation:

---

* The following are the regression statistics:
  $R^2 = 0.197$
  Adjusted $R^2 = 0.185$
  Standard error of X_1 coefficient = 0.022

$$X_2 = -0.001 + .022\ X_1$$

where: X_1 is the logarithm of sales (in thousands)

X_2 is the percent rebate level*

"We found similar regression statistics and coefficients when excluding the milk processors from this model. From this equation we can say that with a 10% increase (or decrease) in sales, a firm can expect an increase (or decrease) of 0.2% in the rebate levels it offers.

"In summary, market power or size of the firm is a more important factor in determining financial performance than it is in determining rebate levels. Rebate levels, which are correlated with sales volume, do not directly explain the variation in financial performance. The correlation levels between rebates, sales volume and financial performance are so low that they do not overturn our previous conclusion that there is no difference in rebate levels offered according to the size of the firm."

---

* The following are the regression statistics:
$R^2 = 0.112$
Adjusted $R^2 = 0.099$
Standard error of X_1 coefficient = 0.007

CONCLUSIONS ON PROCESSORS AND REBATES

The following summarizes my conclusions on the evidence examined in this chapter:

1. Processors are the principal source of rebates in the food industry.

2. Processors offer rebates to retailers and wholesalers in order to sell more products.

3. The bulk of the evidence indicates that there is hard bargaining between processors and retailers on rebates but relations are not coercive. Retailers and wholesalers endeavour to buy as cheaply as possible from suppliers, so as to sell as cheaply as possible to consumers.

4. The small processor (whose sales volume is less than $10 million sales) is having a difficult time financially, particularly during the last three years. The large processor, on the other hand, is earning a reasonable net margin and return on equity.

5. Notwithstanding the conclusion in the paragraph above, there is no significant difference in rebate levels among differing sizes of firms when milk processors are excluded, although there are different patterns of use. Accordingly, there is no support for the theory that rebates are paid as

a resolution of market power measured by the size of the firm, although market power or the size of a processor may be an important factor in financial performance.

6. There is no significant difference in rebate levels offered by suppliers controlled by retailers as compared with those not controlled by retailers.

CHAPTER 6

MILK PROCESSORS AND REBATES

GENERAL

I have decided to devote a separate chapter to milk rebates for three main reasons. First, the level of rebates offered by processors of milk is considerably higher than the level offered by processors of other food products. Second, it is clear from the evidence at the Inquiry that there is serious concern and confusion about the level of milk rebates. Third, there were many allegations and innuendoes concerning milk rebates at the hearings of the Legislative Committee preceding this Inquiry.

DESCRIPTION OF THE FLUID MILK INDUSTRY

Milk has often been described as the nearly perfect food by nutritionists. It contains a balance of most of the nutrients required in the human diet. In this chapter, I will only deal with the fluid milk industry and not with commercial milk. The latter milk is used in various manufactured dairy products such as cheese, butter, milk powder and evaporated milk.

The production and distribution of fluid milk in Ontario is a complex process. I shall endeavour to describe the system simply so that the reader may have a basic background. The system is controlled to a great extent by both the federal and provincial governments.

Ontario dairy farmers, in order to qualify as fluid milk shippers, must meet certain standards established by provincial regulations in respect to farm premises, sanitation and milk quality. Dairy farmers are allocated certain quotas by the Ontario Milk Marketing Board.

The Ontario Milk Marketing Board is a producer organization established under The Milk Act. The Board has been delegated certain authorities with respect to pricing, quotas, pooling, transportation, and other matters relating to the marketing of raw milk. All raw milk in Ontario is marketed through the Ontario Milk Marketing Board.

The Board determines the price which processors must pay for the raw milk. Processors can only buy raw milk from the Board. The result is that all processors buy at a fixed price, so there is no question of rebates at this level. The fluid milk shipper receives a fixed price and does not have to offer rebates in order to market his product.

The Board is responsible for transporting the milk from the farms to the processors. Fluid milk processors (or "dairies" as they are more commonly known) purchase the raw milk, which must contain a certain level of butter fat content. The processors standardize, homogenize and package the raw milk for sale to the wholesaler and retailer. The processor usually sells a variety of by-products of the milk such as cream and buttermilk, as well.

In the past fifteen years, there has been a radical change in the number of dairies in Ontario. In the 1960's almost every small community had its own dairy which delivered milk products to residences. Now the dairies are much fewer in number and the bulk of processing is centralized with very little home delivery. In 1979, there were 78 processors licensed in Ontario* as compared with 198 in 1968.† In 1975, The Independent Milk Distributors Association, which consists of members who deliver milk to the home, had thirteen members. By 1979, Association membership was reduced to nine. At the present time, a relatively small percentage of the fluid milk consumed in Ontario is delivered directly to the home whereas thirty years ago, about 75% was delivered to the home.

Today, the retail store is the main source of milk for the consumer. In addition, the convenience store chains have become major outlets for fluid milk. Some of these convenience stores are controlled by the large milk processors. Examples are: Mac's Convenience Stores, a subsidiary of Silverwood Industries Limited; and Bantam and Astro Variety Stores, subsidiaries of Royal Oak Dairy Limited.

One-stop shopping and low prices at the supermarkets have reduced the appeal of home delivery to the consumer. In addition, technological advances in processing and packaging have increased the shelf life of fluid milk sold in the retail store.

* Ontario Ministry of Agriculture and Food, Annual Report for the Fiscal Year Ending March 31, 1978, p. 49.

† Milk Commission of Ontario, Inquiry on Wholesale and Retail Pricing Practices, Toronto, 1977, p. 7.

Another way in which milk processors may market their products is through non-processor distributors. These are firms which distribute fluid milk products but do not have their own processing plants. Usually they buy milk under contract from the processors and generally they are relatively small firms. They account for a significant share of the remaining home-delivery business and they also supply independent retailers.

HISTORICAL EVOLUTION OF DAIRY REBATES

The evidence at the Inquiry and research by the consultants indicates that the rebate level on fluid milk ranges from about 5% to 30%. The Milk Commission Inquiry on Wholesale and Retail Pricing Practices for Fluid Milk in Ontario, 1971 to 1975 (referred to as the Milk Commission Report, hereafter), reported that, in 1975, "the range of actual discounts was from 15 to 24 per cent" (page 56). Why are milk rebate levels so high relative to other products and why do they appear to be increasing?

We have seen that, originally, dairies offered a high level of service to customers by providing home delivery. The price to the consumer reflected the labour and transportation costs of home-delivery service. Retail stores, naturally, did not require home-delivery service and in lieu thereof, received substantial discounts. This is the historical background of high dairy rebates.

This historical rationale has now taken a minor place behind today's rationale. The major reason today for the

high level of rebating is competitive pricing by the dairies. Competition between dairies has forced each dairy to be extremely price sensitive. A small movement in price by one dairy may result in a large shift in the sales of that dairy and its competitors.

An additional factor that influences the rebate level is savings due to the economies of large scale production. These include the economies of buying, delivery, production and selling. These savings are passed on to the retailer and wholesaler as volume rebates that increase with the volume purchased.

A fourth factor to be considered is that the processors' pricing schedule must be sensitive enough to reflect the differences in service levels between the dairies' customers. The lowest service level is generally experienced in servicing the large customer who receives tractor-trailer loads of milk at his back door. The highest service level is usually experienced in servicing the small customer who may buy much less than a full truckload of milk and who may require the truck driver to fill the store's dairy case.

In summary, the four reasons offered by dairies to explain the evolution of the high level of dairy rebates are:

(1) competition,

(2) present service levels,

(3) economies of scale, and

(4) traditional service levels.

Dairies have not attempted to cost justify the level of rebates for two reasons. First, the expense of carrying out a cost-justification study is prohibitive, and second, more determinants than costs are involved in calculating the dairies' price.

PRICING MECHANISM

The consultants to the Inquiry carried out a thorough investigation of the pricing mechanism utilized by the major dairies in Ontario.

The consultants reported that each dairy publishes a price list. This list indicates the prices of all the fluid milk products sold by that dairy. The list is sometimes called a wholesale price list or, less frequently, a fact sheet. Each dairy also maintains a single rebate schedule. This rebate schedule indicates the level of rebates that may be attained for a given annual dollar volume of purchases. As previously stated, the actual rebate levels range from about 5% to 30%.

There are two main methods by which dairies grant the rebates to their customers. The choice of method to be used is most frequently made by the customer. One method is called the off-invoice method. The dairy calculates the total value of goods sold according to the price listed on the price list. Then, based on the rebate level for which the customer has qualified according to the rebate schedule, the rebate amount is deducted from the price on the invoice and the customer pays the net amount.

The second method is payment of the rebate by cheque. Where this method is employed, the list-price amount is paid by the customer. The dairy then sends to the customer the calculated rebate amount by cheque at a later date. Most small retailers prefer payment of the rebate by cheque while larger customers of the dairies, particularly the chain stores, prefer to use a combination of the off-invoice and cheque methods.

There is a third pricing method that is used infrequently which I call "bargaining on the bottom line." Here, the dairy and its customer agree to a certain price. Billing statements reflect only the negotiated price which the customer pays in full. Rebates play no part in this transaction.

Some dairies offer a volume incentive rebate which is a reward to the customer for increasing his level of purchases by a certain amount over a specified time period, usually one year. The volume incentive rebate payments are generally less than 1% in the dairy industry.

The pricing mechanisms described above apply to fluid milk and fluid milk product sales, such as buttermilk and cream. They do not apply to ice cream and other by-products which are treated like other grocery products having lower rebate levels.

REBATE SCHEDULES AND RETAILERS

As I have stated, each dairy maintains a single rebate schedule. In addition, the dairies publish price lists which are given fairly wide circulation among buyers. When a dairy makes a presentation to a large retailer, part of the presentation usually includes the most current rebate schedule. The dairy assumes that the retailer will not circulate the schedule. In fact, a small retailer seldom receives the rebate schedule. He is usually told specifically what rebate level he qualifies for and is sometimes told at what purchase level the next rebate plateau will come into effect.

This difference in treatment between large and small retailers has resulted in misunderstanding and mistrust among certain small retailers. These feelings are aggravated when the small retailer observes supermarkets selling milk cheaper than he can buy it.

EVIDENCE CRITICAL OF HIGH LEVEL OF REBATES

The Ontario Federation of Agriculture (O.F.A.), in its brief and evidence, was very critical of the high level of rebates in fluid milk. The Federation is of the view that the high level of rebates offered the chains hinders the small retailer's efforts to compete.

To illustrate this, the O.F.A. presented the following chart:

	FOOD CHAIN STORES	SMALL GROCERY STORE
List price - 3 qt. pouch pak 2% milk	$ 1.81	$ 1.81
Less Discount 30%	.54	
Less Discount 6%		.11
Net Cost	1.27	1.70
Selling Price	1.50	1.81
Margin	.23	.11
PCT Margin (of selling price)	15.3%	6.1%

This chart, based on hypothetical values, indicates that the chain stores sell at a price below the small grocery store's cost, thus giving chain stores a tremendous advantage in the market. The O.F.A. further was of the view that this disadvantage has resulted in reducing the volume of sales by small retailers. This reduction, if it leads to business failures, could eventually result in a lack of close-to-home availability of milk, which in turn would have a detrimental effect on the per capita (meaning, per person) consumption of milk.

A second and related concern of the O.F.A. was that the high rebate level in milk will increase the concentration of market power in the chains. The Federation indicated that the trend is to even higher rebates by reference to the findings in the Milk Commission Report, and to its own research.

The O.F.A. also expressed the view that granting large rebates has compelled dairies to increase their wholesale list prices. The effect of this increase is more devastating to the smaller retailer, who cannot offset this increase by the receipt of larger rebates, than to the large retailer. In addition, these large rebates tend to restrict the consumers' choice of brands as a retailer will likely buy only one brand in an effort to maximize its rebate level.

The Independent Milk Distributors Association, already referred to, is an association of nine members. The members sell milk to consumers on a door-to-door basis and also to small stores and speciality shops. The Association, in its brief, disagreed with any economic policy "which promotes the growth and expansion of the large competitors at the expense of the survival of small business in the [dairy] industry." The Association also had strong views on loss-leader selling of fluid milk. This topic will be dealt with in Chapter 14.

Mae Richardson owns a convenience store in Burlington in which she sells milk. She and her husband operate the business, open every day from 8 a.m. to 10 p.m. She has purchased milk from the Borden Company for eleven years, selling milk at cost to induce customers to come into her store. Nevertheless, two years ago, certain chains sold milk at prices below what milk cost her to buy from Borden's. Mrs. Richardson's customers advised her that they thought she was "ripping them off." The situation was given some publicity, and, as a result, Borden's

voluntarily raised her rebate from 5% to 14%. The witness is of the view that there should be one price for milk to all retailers. This incident is also discussed in Chapter 16, Rebates and the Law.

Carl Quaranto is an independent retailer who operates a full-line grocery store of 8,000 to 9,000 square feet in Fenelon Falls. His main competition in the town is an I.G.A. store but he also has competition from chain stores in near-by Lindsay. According to Mr. Quaranto's testimony, the Lindsay A&P was selling three-quart pouch packs of 2% milk for 99¢ during a week in which milk cost him $1.39. Mr. Quaranto buys milk from Kawartha Dairy which gives him a 15% rebate, enabling Mr. Quaranto to earn a profit on its sale. He does not strenously object to rebate levels in milk though he is opposed to loss leadering.

Dr. Stuart Smith, M.P.P. and Leader of the Ontario Liberal Party, submitted a statement and gave evidence in agreement with the O.F.A.'s concerns as to increasing concentration at both retailer and supplier levels of the food industry.

Dr. Smith's evidence may serve as a summation of the evidence critical of discounting, and for this reason, I quote extensively from his testimony below:

> "My concern is, of course, that the situation does seem to exist where because of the discounting practices, the chains are able to sell the milk on some occasions at less than what the

corner store has to pay for it. That's a very real concern and to the extent that the discounting is not truly proportionate to the real benefits of making one delivery rather than two or three and bringing a whole truckload of milk rather than just a couple of quarts,...to the extent that the discounts are more than would truly be reflected by the genuine benefits of delivering in bulk, to [that] extent the corner store is suffering from an unfair trade practice and that's really what I'm trying to remedy with the suggested legislation."

The legislation Mr. Smith refers to is legislation proposed by The Liberal Party to this Commission. This legislation is considered in Chapter 16, Rebates and the Law.

EVIDENCE SUPPORTIVE OF MILK REBATES

1. DOMINION DAIRIES LIMITED

Mr. Charles Scott, President of Dominion Dairies Limited, submitted a brief to the Commission and testified. Dominion Dairies Limited processes a complete line of dairy and frozen dessert products which is marketed to retailers in Ontario and Quebec. Dominion Dairies is estimated by some to be the largest dairy operation in the province. The company markets its products under the brand names of Sealtest and Light 'N Lively. It processes fluid milk and

other dairy products at plants in Toronto, Ottawa, and Windsor, and at one location in Montreal.

I quote extensively from Dominion Dairies' own assessment of the situation:

> "In summary, the experience of Dominion Dairies supports the following conclusions:
>
> 1. Intense competition in the dairy processing and distribution industries in Ontario results in a high degree of efficiency in both processing and distribution, which in turn is reflected in consumer prices for dairy products that compare favourably with prices in most Canadian markets.
>
> 2. There is no evidence whatsoever that the structure of the industry in Ontario is changing in any way that is likely to restrict the availability of dairy products to the consumer.
>
> 3. The introduction of legislated price or discount controls would probably lead to higher profits for large, more efficient processors and to higher prices to consumers. Further, legislated attempts to provide additional choice in the market place is not in the best interests of the consumer due to the dis-

economies of scale which would lead to higher prices as the result of increased costs."

At page 4 of their brief, they deal specifically with discounts:

"Discounts and allowances in the wholesaling of dairy products stem, ultimately, from competition between dairy processors, and are made possible by cost savings resulting from the introduction of economies of scale and other efficiences as volume increases warrant. We have always understood that the way our economic system works, at all levels, is for purchasers to seek the lowest possible prices from their suppliers, which, if the suppliers operate in a competitive market as we do, places them under continuous pressure to perform more efficiently in order to improve quality and to cut costs to remain competitive."

Annexed to the Dominion Dairies brief were several tables which indicate:

(a) that compared to other major centres in Canada and in the United States, the Toronto and southern Ontario consumer is purchasing milk at reasonable prices;

(b) that a comparison of the prevailing prices paid by the consumer for the most popular fluid milk items with the price paid by the dairy processor for raw milk, demonstrates

that the price spread (which means the price difference) between these two prices is lower in southern Ontario than in the other major urban areas in Canada; and,

(c) the number of retail food stores which may be assumed to sell milk increased by 32.3% between 1975 and 1978.

In conclusion, the brief states:

> "...[T]he evidence suggests that at least so far as dairy products are concerned, and given that the cost of raw milk is fixed by The Milk Marketing Board, Ontario's economic system is working exactly in the way it is supposed to work. Real rivalry in an open market place is producing effective downward pressure on costs, resulting in continuing improvements in economies of scale and efficiency, the benefits of which are being passed on to the consumer. The Ontario consumer is getting what he is demanding, and what he has a right to expect, in terms of both an unrestricted supply of high quality dairy products and very competitive prices. He can choose the type of outlet he wishes, and the level which he is willing to pay."

2. <u>DONLANDS DAIRY CO. LTD.</u>

Mr. John Smith, Vice-President in charge of sales for the Donlands Dairy Company, submitted a brief and gave

evidence at the Inquiry. Donlands Dairy Co. Ltd. was founded in 1929 and has grown from a small dairy operating in Toronto to a large enterprise operating dairies in Toronto and Guelph and selling milk and dairy products across southern Ontario. In 1963, it became a wholly owned subsidiary of George Weston Limited. The firm's largest accounts are their affiliated companies, Loblaws Limited and Zehrmart Limited, which are the only chains Donlands sells to, though it also sells to independent retailers and food service outlets.

In the brief, two major submissions are made:

(a) The farmer is not affected by rebates because Donlands, like all processors, pays a regulated price to the Milk Board.

(b) The consumer is not adversely affected by rebating; on the contrary, these discounts reflect the benefits to the consumer from the highly competitive nature of the business.

In summary, Donlands agrees with the conclusion of the Milk Commission Report that the marketing system for fluid milk is relatively efficient, progressive, flexible and equitable.

3. BEATRICE FOODS ONTARIO LIMITED

Mr. Roland Melville Binnington, President, testified on behalf of Beatrice Foods Ontario Limited. This concern

is a private Ontario corporation and a wholly owned subsidiary of the Beatrice Food Company of Chicago. The Ontario corporation processes and markets a full line of dairy products and sells to all levels of the retail trade ranging from supermarkets to the corner grocery store. Beatrice has twelve processing plants in Ontario.

Mr. Binnington was an interesting witness as he has been in the dairy business in Ontario for 37 years. His father had been a farmer outside Kingston, and Mr. Binnington delivered milk in that city for his father. In 1934, when the process of pastuerization was becoming popular, Mr. Binnington's father built a small dairy. In the 1960's, this dairy merged with another local dairy as the result of which a new processing plant was constructed. In 1969, this company sold its operations to Beatrice Foods. In fact, the twelve processing plants now owned by Beatrice Ontario were formerly small dairies. Despite the change in ownership, the original owner still manages the dairy in many cases. The company has approximately 40 franchisees who purchase Beatrice products. In some cases, the franchisees are small dairies which for various reasons decided to discontinue processing operations. In other cases, the franchisees are individual routemen distributing Beatrice products.

One of the main reasons that the number of dairies has decreased, Mr. Binnington testified, is due to government regulation; metrification, for instance, involves extraordinary cost to dairies. The witness indicated that it is

difficult for small dairies to obtain funds critical to modernization and expansion.

Mr. Binnington testified that rebates have increased since 1978. Beatrice Ontario does not negotiate rebates varying from its wholesale price list or rebate schedule. The dairy makes a presentation to a retailer which may choose to accept or reject it. The dairy also offers rebates with respect to co-operative advertising, and has taken part in promotional allowances. The company has also sold dairy equipment to retailers at cost and, at times, has given loans to them.

Beatrice Ontario is able to offer larger rebates to the chains due to certain efficiencies in making a large volume delivery, whereas it is often necessary to service the dairy counters in supplying a smaller firm.

It was this witness's opinion that small dairies can offer the same volume rebates in their local area as his firm can. Mr. Binnington testified that, at the date of his testimony, there were five major dairies in Ontario competing with one another: Borden's, Silverwood's, Dominion Dairies, Beatrice and the combination of Donlands and Clark Dairy owned by George Weston Limited.

4. SILVERWOOD DAIRIES LIMITED

Mr. Michael Earl Duffy, the President of Silverwood Dairies Limited, testified on behalf of the corporation. Silverwood Dairies Limited is a wholly owned subsidiary of

Silverwood Industries Limited; Mac's Milk is also a subsidiary of Silverwood Industries Limited. Silverwood's is a Canadian-owned company and carries on business in several provinces. The firm has four processing plants in Ontario located in Toronto, Peterborough, North Bay and London.

Silverwood Dairies processes a full line of dairy products. In Ontario, the company sells mainly to the small- and medium-sized independent supermarket groups, and in addition, has a fair-sized network of franchise operators and distributors. Silverwood's is the main supplier of milk to the Mac's Milk Stores, which, although a sister company, is separately managed.

Mr. Duffy indicated that Silverwood Dairies' volume rebates ranged from 15% to 25%. He further observed that competition is keen between processors. The witness was unable to explain why Silverwood's could not obtain the business of the major chains.

5. STONEY CREEK DAIRIES

Mr. Gregory George Dawson, President, gave evidence on behalf of Stoney Creek Dairies. The firm had a single processing plant located in Stoney Creek, Ontario, at the time of the hearings. Stoney Creek's fluid milk processing business was subsequently sold to Royal Oak Dairy Limited of Hamilton. Annexed to the plant was a variety store, ice cream parlour, and restaurant. This complex, in total employed 55-60 persons and was a much smaller operation than the dairies referred to above.

Stoney Creek, like the larger dairies, had a rebate schedule which was not published, but was shown to variety stores. This dairy's volume rebates averaged 15%.

Mr. Dawson testified that he is not opposed to rebates in and of themselves. Rather, the witness recognizes that rebates are the result of economies. However, his firm was finding it harder to compete as rebate levels increased. He pointed out that his customers, mainly small retailers, could not sell milk as cheaply as the chains because they could not buy it from dairies as cheaply. I thought most interesting Mr. Dawson's evidence that he would be able to match the rebate levels offered by the larger dairies provided he could obtain a chain store contract.

1. NATIONAL CITIZENS' COALITION

Dr. Arnold Aberman, testified and submitted a brief on behalf of the Citizens' Coalition. Dr. Aberman is an Associate Professor of Medicine at the University of Toronto and Physician-In-Chief at Mount Sinai Hospital in Toronto. In addition, he and his wife operate a publishing company for which they received the Canada Enterprise Award in 1975. Dr. Aberman has acted as a consultant with the Fraser Institute, Vancouver, for its studies on free markets. Dr. Aberman endeavours as a private citizen to influence public policy by education. He has written articles on marketing boards and given interviews on the subject on television and radio.

The Citizens' Coalition is a group of Canadian citizens, including approximately 20,000 paying members, concerned about matters of public policy. One of the group's major concerns is the amount of government regulation; the Coalition supports instead competitive markets free of government regulation.

I now summarize the parts of the Coalition's brief which are relevant to milk rebates:

1. That part of the food industry which can be characterized as a free-market competitive system has benefitted the Canadian public.

2. The retail sector, in particular, has an excellent record.

3. As reported by the federal Department of Consumer and Corporate Affairs in Working Paper #2, "Application of Competition Policy to the Food and Agricultural Sector,"*
   (a) the combined profit margin of the wholesale and retail sectors is only 2 1/2% on average; and,
   (b) there are several problems prior to the sale of product to the retailer, particularly with respect to agricultural products that are subject to supply-management regulation by marketing boards.

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* Bureau of Competition Policy (Ottawa: July, 1978), p.4.

4. Present discounting practices are beneficial to farmers, wholesalers, retailers and consumers in that these practices promote efficiency in the food distribution system.

5. The supply and prices of basic agricultural products are increasingly controlled by monopolistic marketing boards; these boards are operating to the detriment of the consumer.

6. A general policy of marketing boards is not to allow rebates, regardless of the efficiencies they may introduce.

7. If a policy of allowing discounts and allowances at the farm gate were to be established, and if the individual farmer were allowed to make his own decision concerning pricing and production policies, Ontario would have a more efficient food production system and both the farmer and consumer would gain.

7. RETAIL STORES

Officers from Dominion Stores, Loblaws, Steinbergs, A&P, Canada Safeway, I.G.A. and Knob Hill Farms testified in relation to milk rebates. Their evidence was similar in many respects and for this reason, I shall summarize it.

1. Milk rebate levels range from 25% to 30%. Mr. Nichol of Loblaw's testified that his firm

received rebates of 25% to 30% off the wholesale list price. He described this list price, however, as "completely fictitious" as this is the price which a small restaurant that requires costly daily service must pay. Knob Hill indicated it received 25% to 30% rebates on milk plus tractor-trailer-load allowances of 5% to 6%. Not all retailers receive milk rebates, however; Canada Safeway does not receive rebates but purchases milk from Dominion Dairies at a bottom-line price. On the other hand, A&P indicated that it purchased from fourteen dairy processors of which only one, Borden's, sold at a bottom-line price.

2. Most retailers felt that the rebates are cost reductions earned by the services that retailers provide and by the savings that suppliers experience.

3. Retailers may sell milk at a reduced price by not taking their usual profit. For example, Mr. Nichol testified that Loblaws only makes 10% to 12% mark-up on milk, whereas it requires a mark-up of 20% to 23% on most products to obtain an overall profit considering their costs.

4. Competition is very keen among processors to sell milk to the chains. Conversely, all retailers endeavour to purchase milk at the lowest possible net cost from the dairies.

8. BUYING GROUPS

Mr. Ralph Moyal, the General Manager of Independent Wholesale Grocers Limited (I.W.G.L.), testified on his company's behalf. I.W.G.L. is a buying group made up of wholesalers and retailers. The main purpose of I.W.G.L. is to purchase in volume in order to maximize the volume rebates which members can obtain. The company consolidates orders for its members though the products are delivered directly to the member.

Mr. Moyal testified that I.W.G.L. received a 25% rebate off the list price for milk from Borden's Dairy. If the I.W.G.L. member picked up supplies from the Borden plant, that member received another 5% rebate. In addition, a member could earn a further 3% volume discount. Therefore, a member might have earned a total discount of 33%.

9. MILK COMMISSION OF ONTARIO

Mr. James F. Jewson, the Vice-Chairman, testified on behalf of the Milk Commission of Ontario. The Milk Commission was established by The Milk Act, 1965 (R.S.O. 1970, c. 273) and its powers and duties are set out in section 4 of that Act. The Milk Commission has jurisdiction to do the following, amongst other things:

(a) to inquire into any matters relating to the production, processing or marketing of milk;

(b) to stimulate, increase and improve the marketing of milk and milk products;

(c) to co-operate with marketing boards;

(d) to prepare legislation concerning quality standards for milk;

(e) to administer the fund for milk and cream producers.

The Commission is responsible to the Minister of Agriculture and Food.

In 1975, the Minister required the Commission to conduct an inquiry into the fluid milk industry of Ontario. Three of the terms of reference for The Milk Commission Inquiry are particularly relevant to the present Inquiry. They are:

"1. To investigate pricing practices and margins between processors, distributors and retailers of fluid milk;

2. To inquire into discounting practices in and after the year, 1972;

3. To compare the retail margins and practices in Ontario with those in other jurisdictions."

The Inquiry conducted extensive hearings and research, and reported to the Minister in 1977.

The principal recommendations of the Milk Commission Inquiry, as they relate to my Commission, are, in summary form:

1. that, in general, the marketing system for fluid milk is relatively efficient, progressive, flexible and equitable;

2. that there should be a continuing assessment of the effect of changes taking place in the structure of the processing, distributing and retailing sectors of the fluid milk industry and that appropriate action should be taken to correct any harmful practices which are found to exist.

Mr. Jewson was not aware that discounts had increased since the Milk Commission Inquiry. He stated that the Milk Commission has not been asked to monitor on a continuing basis the types and amounts of discounts. Upon cross-examination by counsel for the Ontario Federation of Agriculture, he admitted that The Milk Commission did have jurisdiction to investigate discounts but he submitted that the Commission did not have the staff to carry out such an investigation.

PROFIT AND EQUITY POSITION OF MAJOR DAIRIES

I asked the consultants to provide me with financial data relating to four major dairies in Ontario in order to resolve the conflict in testimony on this subject. The figures produced below for gross margin, net margin and the returns on equity, are the average of the four firms. The data is presented as an average in order to protect confidentiality of the firms involved.

FOUR MAJOR ONTARIO DAIRIES

FINANCIAL STATISTICS

(Latest fiscal year end prior to 1 Jan., 1979)

Sales Volume	Gross Margin	Net Margin (after tax)	Return on Equity (after tax)
$30 million to $200 million	19.8%	1.5%	15.5%

These figures indicate a profit margin of 1.5% on sales, which is low relative to other processors, whereas the return on equity is comparatively healthy at 15.5%. These returns indicate that the high level of rebates is not associated with abnormally high or low profit levels.

CONCLUSIONS

The following summarizes my conclusions on the evidence examined in this chapter:

1. All raw milk in Ontario is marketed through the Ontario Milk Marketing Board. This Board establishes the price that milk processors are obliged to pay for the purchase of milk. As a result, the fluid milk shipper (the dairy farmer) does not offer rebates to market his product.

2. The number of dairies in Ontario has declined dramatically in the past 15 years as processing has become more centralized. Consumers now purchase their milk mainly from retailers and seldom by way of home delivery.

3. The rebate level on fluid milk offered by processors has increased significantly in the past few years to the point that volume rebate levels in 1979 ranged from 5% to 30%.

4. The major reason for the high level of rebates is price competition among the dairies. An additional reason is the savings due to large scale production. Dairies do not cost justify their levels of rebates, due to the expense of such a study.

5. A small retailer cannot buy milk as cheaply as a large retailer and consequently is at a disadvantage. Nevertheless, there has been no reduction in the number of outlets where a consumer can purchase milk.

6. Large retailers sell milk, in certain cases, at a loss or at a reduced price. Consumers are benefitting from the intense competition at both the processing and retailing levels.

7. A profit and equity survey of the four largest dairies indicates a low profit margin on sales of 1.5% and a reasonable return on equity of 15.5%. Therefore, payment of very high rebates by dairies does not appear to be associated with abnormally low (or high) profit levels among these processors.

8. I agree with the conclusion in the Milk Commission Report of 1975, that "in general, the marketing system for fluid milk is relatively efficient, progressive, flexible and equitable". However, I would suggest that the Milk Board should continually monitor the milk industry from dairy farmer to retailer to ensure that no serious aberrations develop.

CHAPTER 7

BUYING GROUPS AND REBATES

GENERAL

The significance of rebates is clearly illustrated when one considers the buying groups in the food industry. One can state with a reasonable degree of accuracy that buying groups would not exist if it were not for volume rebates.

In the public's mind there is some confusion as to the function and purpose of buying groups. Accordingly, in this chapter, I shall endeavour to explain the purpose of buying groups. I shall also attempt to explain how they treat rebates.

THE NATURE OF BUYING GROUPS

Buying groups consist of wholesalers and retailers who unite to establish a purchasing firm with the purpose of maximizing volume rebates.

There are seven major buying groups that have members doing business in Ontario. These are:

Foodwide of Canada (1977) Limited

Independent Wholesale Grocers Limited [I.W.G.L.]

Independent Grocers Alliance [I.G.A.] Canada Limited

International Tobacco Wholesalers Alliance Limited [I.T.W.A.L.]

United Grocery Wholesalers Limited [U.G.W.L.]

Intersave

Retail Merchants Association of Canada (Ontario) Incorporated

Appendix 3 indicates the wholesalers and retailers which are members of the first six buying groups.

All buying groups are legal entities separate from the members except for Intersave. Intersave is a division of Loblaw Companies Limited (Toronto).

Dominion Stores, Steinberg and Safeway are major retailers in Ontario which do not belong to buying groups. One can conclude from this that their volumes of purchases are sufficiently large to enable them to procure high volume rebate levels on their own, without associating with other firms in a buying group.

The Inquiry consultants researched all the buying groups that have members carrying on business in Ontario. I have relied heavily on their research in the paragraphs that follow.

There are two types of buying group operations in Canada. Type 1 buying groups exist primarily to take advantage of volume rebates on name brand products. By pooling purchases, the members of a buying group move to higher levels on the volume rebate scales offered by suppliers. For example, suppose three companies each purchase $200,000 worth of goods and receive rebates of $2,000, being 1% of purchases. If the three companies pool their purchases in a buying group, the combined purchases of

$600,000 may qualify for a volume rebate of $12,000 being 2% of purchases. Thus, each company's share of the rebate will be $4,000 or double the original rebate.

Type II buying groups act as managers for the members' purchases of house brand products and no-name products. These groups may negotiate contract terms including price levels, co-ordinate production levels (where several suppliers of house brand products may be involved), and perform product testing and quality control. Usually the rebate received by this type of group is an agent's fee, rather than a volume rebate. Generally this type of buying group saves considerable duplication of services by coordinating the members' purchasing efforts.

While most buying groups' operations are either one type or the other, there are several that are combinations of both types. I.W.G.L., U.G.W.L., Foodwide and I.T.W.A.L. are Type I buying groups. I.G.A. and Intersave combine the characteristics of Types I and II.

Several buying groups have in common the fact that they do not take delivery of the goods purchased; instead, the goods are shipped directly to the group members. Another common feature is that buying groups purchase only on behalf of members, all members being shareholders in the buying group. Members may be retailers or wholesalers or both. Another common feature is that the buying group is liable to suppliers for accounts not paid by members.

Membership requirements of buying groups vary for each group. Some groups require that all members share a common ownership bond. Other groups require no ownership links but require financial stability and ownership of a warehouse. The financial requirement is due to the fact that the buying group assumes responsibility for its members' purchases. Ownership of a warehouse is mandatory in some cases because the group itself does not take delivery of goods. These requirements may impose hardship on a small retailer or small wholesaler wishing to become a member of a buying group.

Mr. Ralph Moyal, the General Manager of I.W.G.L., testified before the Inquiry. He gave evidence that I.W.G.L. has been in existence for 65 years. Annual total retail sales of I.W.G.L. members approximate $700 million.

Mr. Moyal testified that it is difficult for a new wholesaler to become a member of the group. An applicant has to provide financial statements for five years indicating progress and stability. The applicant must also own a warehouse. In addition, the applicant must meet the minimum annual sales requirements of $10 million. Finally, the prospective member must have more than one retail outlet.

According to the witness's testimony, rebates received by I.W.G.L. and passed on to member companies are most important to the financial success of those companies. In many cases, these rebates represent the difference to a member between making a profit or showing a loss. The

amount of volume rebates received by Ontario members in 1978 was $673,795.76, as shown in an exhibit filed by Mr. Moyal.

Mr. Moyal's testimony as to the importance of buying groups was supported by the testimony of other witnesses.

Mr. J. Donald Tigert, an investment expert specializing in the food industry, testified that independent retailers who are members of voluntary buying groups are able to retain their share of sales in the Ontario market.

Mr. Jack Levine, the President of Steinberg's, a firm which does not belong to a buying group, testified that buying groups create an unfair advantage. It was his opinion that volume rebates paid to buying groups are not based on considerations of efficiency. He posed the example that a supplier to a buying group might have to deliver to twenty warehouses whereas the same supplier only has to deliver to two Steinberg warehouses although both the buying group and Steinberg may achieve the same rebate.

BUYNG GROUPS' FINANCIAL CHARACTERISTICS

As previously indicated, our consultants surveyed all the buying groups with operations in Ontario. The consultants concluded that all are operating on a non-profit basis. This is achieved by the group's distributing all revenues, less costs of operation, to the members in proportion to each member's purchases.

The operating procedures for each buying group differ slightly from group to group. Some groups charge membership fees equivalent to or in excess of all operating costs and then pay 100% of the rebates received, together with any surplus, to the members. Other groups charge nominal membership fees and pay operating costs from the rebate amounts received before disbursing the remainder to the members.

It is the consultants' opinion, supported by the evidence heard, that payments to members represent direct pass-through of rebates from suppliers to buying group members. "Pass-through", as used in this report, means that the rebates in question are transferred from one link, through a second link, to a third. In this case the rebates are passed from the suppliers through the buying group to the group's retailer and wholesaler members, with no more than minimal deductions.

BUYING GROUPS AND REBATES

The rebates received by Type I buying groups are exclusively volume rebates. Our consultants' research indicated that the majority of buying groups qualify for rebates at or very near the top of most volume rebate scales. The general range of rebates received by Type I buying groups is from 1% to 5% of purchases.

Rebates received by Type II buying groups, those which deal heavily in house brand and no-name products, are usually brokerage or special allowances. Type II buying

groups qualify for these allowances by performing services such as label design and product testing which would otherwise be performed at the expense of the supplier granting the allowances. The general range of rebates received by Type II buying groups is from 1.5% to 3% of purchases from suppliers.

The most important result of these rebates is that the percentage level of rebates for all members of buying groups is approximately the same, regardless of the size of individual members. For example, if a buying group's volume rebate from a particular supplier was 5%, a member with purchases of $100,000 will receive a 5% rebate, or $5,000; similarly, a member with purchases of $10,000 will receive a 5% rebate, or $500. Without the buying group, the member with purchases of $100,000 may not have qualified for the 5% rebate and the member with purchases of $10,000 almost certainly would not have qualified for this rebate level.

The significance of this result will become apparent in Chapter 9, Large Retailers, Consumers and Rebates, and in Chapter 10, Small Retailers and Rebates.

CONCLUSIONS

1. Buying groups are formed by buyers to obtain the highest possible level of volume rebates from suppliers.

2. Except for a few large retailers who have sufficient purchasing power on their own, an important number of retailers in Ontario purchase through a buying group or from a member of a buying group.

3. Buying groups eliminate most differences in levels of volume rebates due to volume-purchasing differences between large and small retailers and wholesalers.

4. It may be difficult for a small retailer or a small wholesaler to become a member of a buying group because of the group's membership requirements.

5. Rebates received by buying groups from suppliers are passed through to members, and the groups operate on a non-profit basis.

6. The amount of volume rebates paid to buying groups may not correspond to the cost savings of volume ordering. The implications of this conclusion are stated in the following paragraphs.

7. The percentage level of volume rebates for all members of buying groups is approximately the same, regardless of the member's size.

8. The percentage level of volume rebates for buying group members may be similar to the level of volume rebates for the large chains which are not buying group members.

CHAPTER 8

WHOLESALERS AND REBATES

DEFINITION

Wholesalers are the intermediate link between the processor and the retailer. A wholesaler purchases a product in large quantities, warehouses the product and then sells to retailers on demand.

METHODS OF SELLING

There are two types of wholesaler selling operations.

The traditional type operates pursuant to an order system, whereby the customer orders goods which the wholesaler delivers to the retailer's place of business.

The newer type of wholesale operation is called "cash and carry". The customer attends at the warehouse, orders and pays for his goods, and transports the goods from the warehouse to his store.

CUSTOMERS OF WHOLESALERS

Customers of wholesalers fall into two general categories: wholesaler-sponsored retailer or independent retailer.

Wholesalers that sponsor retailers are listed in Table 8-A. This type of retailer is most often a member of a

chain, voluntary or otherwise. Sponsorship aid to the sponsored retailer may simply consist of general merchandising assistance or it may involve a complete package of services including pricing-policy assistance and profit planning. Underlying the sponsorship is often a financial bond, ranging from wholesaler-controlled retail franchises, to wholesaler-supplied loans, to direct wholesaler ownership of the retail outlet.

Wholesaler-sponsored retailers represent a significant part of the retail food industry. Table 8-A alone identifies sponsorship of 1,670 retail stores in Ontario. A group-sponsoring wholesaler often offers pre-printed forms for ordering and advertising, and assistance in advertising planning. It may also offer meat- and produce-buying programs. Some wholesalers offer assistance to retailers in the form of guarantees on leases and store-location advice.

The second category of wholesale customer is the independent retailer who is not affiliated with the wholesaler. This retailer may be affiliated with another level of the food chain. For example, the Becker chain of convenience stores buys milk from its affiliated dairy and buys most other groceries from an unaffiliated wholesaler, National Grocers.

TABLE 8-A

GROUP SPONSORING WHOLESALERS: ONTARIO OPERATIONS

This table gives the following information about group-sponsoring wholesalers:

Company Name, Central Area of Operation
- Name of retail operations sponsored, number of stores operated.

****

Elliott Marr & Co., London
- Superior, 46 stores
- United Buyers, 70 stores

Knechtel Wholesale Grocers, Ltd., Kitchener
- Knechtel Associate Stores, 18 stores
- Knechtel Food Markets, 2 stores
- L&M Food Markets, 8 stores

M. Loeb Ltd., Ottawa, London and Sudbury
- I.G.A., 104 stores
- Muchmore, 33 stores
- Pinto, 87 stores
- Box Stores, 2 stores

Lumsden Brothers, Ltd., Burlington
- Foodland, 17 stores
- Clover Farm, 17 stores
- Best Valu, 160 stores

National Grocers Company Ltd., Headquarters in Toronto, branches across Ontario
- Red and White, 175 stores
- Supersave, 41 stores
- Lucky Dollar, 106 stores
- Maple Leaf, 484 stores
- Marché Suprime, 25 stores
- OK Economy Markets, 2 stores

The Oshawa Group, Ltd., Toronto
- I.G.A., 142 stores
- Ranch, 4 stores
- Food Town and "A" accounts, 100 stores
- Jug City, 17 stores

****

SOURCE: Canadian Grocer, August, 1979.

SIZE OF THE ONTARIO WHOLESALE MARKET

The Ontario wholesale food market had approximately $4.0 billion sales in 1979.* No figures are published on the number of food wholesalers operating in Ontario. The 1971 census indicated there were 1,021 wholesale locations in Ontario and industry sources estimate that there are at least that number today.

Table 8-B lists the Ontario sales of the 21 largest firms that derive a substantial portion of their sales from grocery wholesaling; in some cases, these figures include sales of non-food products, retail sales, sales outside Ontario, or brokerage sales. Sales of these 21 companies account for approximately $1.9 billion of 1977 Ontario wholesale sales, or 58% of the estimated 1977 Ontario wholesale sales of $3.3 billion.*

CONSULTANTS' SURVEY OF WHOLESALERS

The Inquiry consultants surveyed a cross-section of the wholesale business in Ontario. The sample ranged from small firms experiencing sales of less than $20 million to large firms with sales of more than $1 billion.

All the wholesalers surveyed operated on net after-tax profits of less than 1% of sales. The return on equity for the entire sample varied from 5.8% to 15.9%. These returns

* Estimate derived from Statistics Canada Catalogues 97-702, 97-722 and 63-008, and _Canadian Key Business Directory_, Dun and Bradstreet, 1979.

TABLE 8-B

WHOLESALE SALES OF ONTARIO FOOD WHOLESALE FIRMS - 1977

COMPANY	WHOLESALE SALES ($000,000)
M. Loeb, Ltd.	581.7
The Oshawa Group	542.8
National Grocers, Ltd.	542.4
Stuarts Branded Foods, Ltd.	41.9
Lumsden Brothers Ltd.	40.0
UBA Trading Co. Ltd.	34.4
Hickeson Langs Supply Co. Ltd.	31.0
Young - Warren Food Brokerage	25.0
Grant Small Sales, Ltd.	24.0
Lanzarotta Wholesale Grocers Ltd.	20.0
Nathaniel Gibbs Canada, Ltd.	20.0
Mike's Supermarket 1962, Ltd.	20.0
Knechtel Wholesale Grocers Ltd.	18.2
Gamble Robinson, Ltd.	15.6
Smith and Whittaker Food Brokerage	15.0
Elliott Marr & Co. Ltd.	14.8
C.B. Powell, Ltd.	14.0
H. Fine and Sons Ltd.	13.5
Bennett's Foods, Ltd.	11.6
Alex Smith Sales, Inc.	11.0
A.S. May and Co. Ltd.	10.0
TOTAL	1,904.5

SOURCE: The above figures are estimates derived from: Dun and Bradstreet, 1979 Canadian Key Business Directory, and published corporate financial reports.

are not correlated to sizes of sales. The returns on equity for the entire sample vary during the last three years, showing a definite increase in each of the last two years.

WHOLESALERS AND REBATES

Generally stated, all wholesalers receive rebates similar to those received by retailers. These rebates include co-operative advertising allowances for which performance may be publication of a flyer in the order book or a sign on the shelves. In many cases, co-operative advertising will be supplemented by an off-case allowance which the wholesaler is expected to pass through directly to his customers in the form of a reduced price. Most wholesalers belong to buying groups, as explained in the previous chapter, and qualify for increased volume rebates from this association. Fixed-rate rebates, such as promotional allowances, are paid to all wholesalers regardless of size.

Rebate levels for wholesalers average from 5% to 7% of purchases from suppliers. These figures consist of rebates received by cheque which are disclosed on the wholesaler's books of account plus off-case allowances which are estimated.

ACCOUNTING TREATMENT AND PASS-THROUGH OF REBATES

The term "pass-through", as I have explained earlier, refers to the flow of rebates from one link in the food

chain to the next without substantial reduction. Wholesalers use three methods to pass rebates through to retailers. These methods are explained below and hypothetical income statements are presented in Table 8-C illustrating each method.

Method I is a direct pass-through by a reduction in the cost of goods. Thus, if a supplier grants to the wholesaler a trade allowance in the amount of $2 less per case, the wholesaler sells the item at $2 less per case to his customers. This method is used particularly for off-invoice and off-case allowances such as trade allowances and truckload allowances.

Method II is an indirect pass-through according to which the wholesaler applies rebates received against his operating expenses. Thus, the rebate reduces the amount of selling, general and administrative expenses which the wholesaler must defray. These costs would otherwise be provided for by an upcharge or markup which would add to the selling price charged to the retail customer. In some cases, wholesalers using this method have not increased this upcharge for ten years because increased expenses have been balanced by increased rebates.

Method III is an infrequently used direct method of pass-through. According to this method, the wholesaler pays his customers directly by annual cheque in the amount of the volume or promotional rebates he receives by cheque. Rebates are treated as revenue in the wholesaler's books of account in this case.

TABLE 8-C

WHOLESALER ACCOUNTING TREATMENT OF REBATES

METHOD I			METHOD II			METHOD III		
Sales Revenue and Total Revenue		100	Sales Revenue and Total Revenue		100	Sales Revenue	106	
Gross Cost of Goods Sold	96		Gross Cost of Goods Sold	96		plus Rebate Revenue	6	
less Rebates received	6					Total Revenue		112
Net Cost of Goods Sold		90	Net Cost of Goods Sold		96	Net Cost of Goods Sold		96
Gross Income		10	Gross Income		4	Gross Income		16
Selling, General and Administrative Expense		9	Selling, General and Administrative Expense	9		Selling, General and Administrative Expense	9	
			less Rebates received	6		plus Rebates paid out	6	
			Net Expense		3	Net Expense		15
Net Income		1	Net Income		1	Net Income		1
Markup (Sales Revenue - Net Cost of Goods Sold)		10	Markup		4	Markup		10
						Gross Cost of Goods to wholesaler's customer	106	
						Rebates paid to customer	6	
Net Cost of Goods to wholesaler's customer		100	Net Cost of Goods to wholesaler's customer		100	Net Cost of Goods to wholesaler's customer		100

The pricing practices for the various methods are as follows:

In Method I, the wholesaler records \$90 as his net cost of goods, deducting rebates received (\$6) from the amount he is billed by his supplier (\$96). The wholesaler wishes to earn \$1 of profit and he must defray \$9 of expenses, so he adds a markup of \$10 to the \$90 net cost when billing his customer, the retailer. This sum of \$100 (\$10 plus \$90) is recorded as the wholesaler's sales revenue and total revenue.

In Method II, the wholesaler records \$96 as his net cost of goods, being the amount he is billed by his supplier. The wholesaler chooses to deduct rebates received (\$6) from the amount of expenses he must defray (\$9), leaving only \$3 of expenses to be defrayed. The wholesaler again wishes to earn a profit of \$1, so he adds a markup of \$4 to the \$96 net cost when billing his customer. This sum of \$100 (\$4 plus \$96) is recorded as the wholesaler's sales revenue and total revenue.

In Method III, the wholesaler records \$96 as his net cost of goods, as in Method II. As in Method I, the wholesaler wishes to earn \$1 of profit and he must defray \$9 of expenses. Accordingly, he adds a markup of \$10 to the \$96 net cost when billing his customer. This sum of \$106 (\$96 plus \$10) is recorded as the wholesaler's sales revenue. When the wholesaler receives the rebate (\$6) he chooses to record it as revenue, making his total revenue \$112 (\$106

plus $6). Once the rebate is paid to the customer, it is recorded as an expense.

The above is a simplification of the formal accounting treatment. It must also be stressed that day-to-day pricing decisions in the real world are based on other factors in addition to costs and expenses, but the over-all or long-run considerations are as they have been explained above.

The particular method chosen by the wholesaler is usually determined by accounting tradition and ease. It is important to note that the wholesaler makes the same net income or profit and sells at the same price regardless of the method of accounting and pass-through. The question as to what happens to a rebate if it is not passed through directly is resolved by noting that all rebates are passed through, if not directly, then indirectly in the form of defrayed expenses. The consultants' survey results indicate that most retailers use both Methods I and II at the same time, in differing proportions.

CONCLUSIONS

The following summarizes my conclusions as to the evidence examined in this chapter:

1. Wholesalers play a major role in the distribution of food. The Ontario wholesale food market accounted for approximately $4.0 billion in sales in 1979.

2. The sales of the 21 largest wholesale firms accounted for $1.9 billion of 1977 Ontario wholesale sales, or 58% of the estimated $3.3 billion of sales by all wholesalers.

3. Wholesalers surveyed operated on net after-tax profits of less than one per cent of sales. The surveys showed wholesalers' returns on equity varied from 5.8% to 15.9%. These returns are similar to those of other similar industries and indicate that rebates are not associated with abnormally low or high profits at the wholesale level.

4. Rebate levels for wholesalers averaged from 5% to 7% of purchases. These figures include estimates of off-invoice allowances.

5. All rebates received by wholesalers appear to be passed through, either directly or indirectly, to the retailers.

6. The size of rebates paid to the wholesaler does not seem to be directly related to the size of the wholesaler.

CHAPTER 9

LARGE RETAILERS, CONSUMERS AND REBATES

GENERAL

A major term of reference for the Inquiry to answer is the effect of rebating practices on prices to the consumer. It is in this chapter that this term of reference will first be directly addressed.

In previous chapters, I have considered rebating practices in relation to the producer, importer, processor, wholesaler and buying groups. The scheme of the Report is to follow the food product through the food chain from producer to consumer. In colloquial language, the retailer represents the "end of the line" in the food chain as it is the retailer which sells the food product directly to the consumer.

The Inquiry hearings and consultants' investigations were directed to answering the following questions in regard to retailers:

(a) What effect does rebating have on prices paid by consumers?

(b) Are rebates passed through to the consumer?

(c) Are retailers using the revenue from rebates to pay for increased expenses caused by inefficiency?

(d) Are the retailers' margins of profit related to rebates?

(e) Are the retailers' returns on equity related to rebates?

(f) Is there real competition between retailers?

CONCENTRATION

The retail segment of the Ontario food industry is moderately to highly concentrated. I will explain this finding in more detail in Chapter 13, Concentration and Rebates. It is sufficient to state here that the retail chain stores account for a significant proportion of food sales. One trade publication has estimated that retail chains, including the convenience store chains, account for 73% of food store sales in Ontario, and 60% in Canada.*

Mr. J. Donald Tigert, one of Canada's leading financial analysts in the food industry, gave expert testimony on the state of the industry to the Inquiry and I have drawn heavily on his evidence in forming my conclusions. In particular, he provided the estimates of market share for 1978 retail food sales in Ontario printed in Table 9-A. This table will also be discussed in Chapter 13 which considers the effect of rebates on concentration. The next chapter considers the small food retailers and rebates.

CONSULTANTS' SURVEY

The Inquiry consultants surveyed large and small retail chains, adopting the Statistics Canada definition of a "chain" meaning four or more commonly owned establishments.

* Canadian Grocer, February 19, 1979.

TABLE 9-A

ONTARIO FOOD STORE MARKET SHARES

Company	Estimated Share of Market
Dominion Stores	
Dominion	21.0%
Hiway Market	0.3%
Bittner's	0.4%
TOTAL	21.7%
Loblaw Companies	
Loblaw	11.9%
Zehr/Gordon's	3.6%
Ziggy's	0.2%
National Grocers (wholesale)	6.0%
TOTAL	21.7%
Steinberg Inc.	
Miracle Mart	9.1%
Oshawa Group	
Food City	3.6%
Dutch Boy	0.5%
I.G.A. (wholesale)	3.1%
TOTAL	7.2%
A&P Canada	6.0%
M. Loeb Limited	6.0%
Canada Safeway	2.7%
Becker Milk	2.3%
Mac's Milk	1.8%
All other food stores	21.5%
GRAND TOTAL	100.0%

SOURCE: Estimates by J. Donald Tigert, Burns Fry Limited.

The questionnaire reprinted in Appendix 5 was forwarded to seven large retail chains and nine smaller chains in Ontario and the data received in response was examined and checked before inclusion in the consultants' report. The larger chains include the well-known national supermarkets while the other group surveyed consists of minor supermarket and convenience store chains which nevertheless may consist of many small outlets.

SALES STATISTICS

Table 9-B shows a breakdown of retailers by size of operations. The average sales volume among the large chains was $1,149.5 million. Sales ranged in dollar value from approximately $190 million to over $2 billion. The average sales volume among the small chains was $40.5 million; sales ranged from $1.5 million to $140 million.

OPERATING MARGINS

Figure 9-A depicts the latest operating margins for small and large chains surveyed. The figures represented were obtained from audited accounting statements for fiscal years ending during 1977.

It is significant from the standpoint of rebating that the cost of sales in the two groups is almost the same, totalling 78.9% for the small chains as compared with 80.0% for large chains. The profit levels of 1.1% for large chains and .9% for small chains show little significant difference.

TABLE 9-B

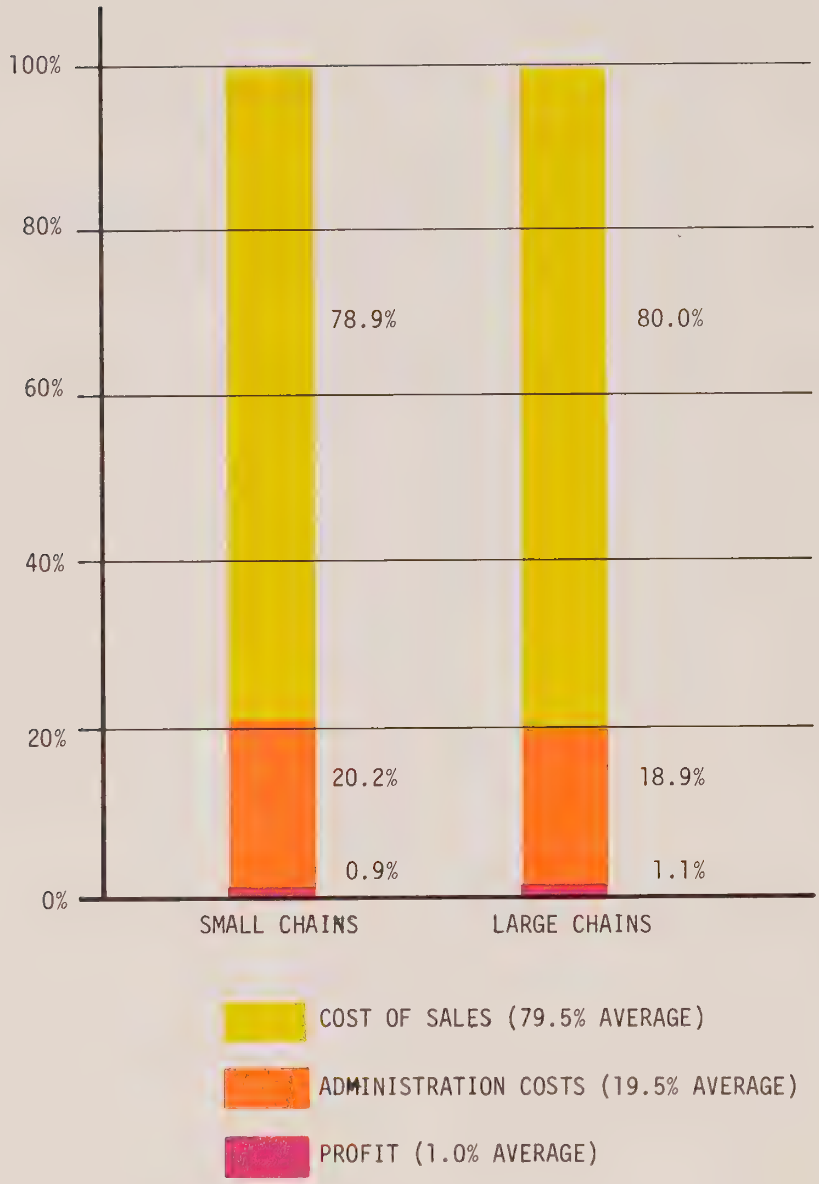
BREAKDOWN OF RETAILERS BY SIZE OF OPERATION

Size of Operation	Number in Sample	Average Sales
Small chains	9	$ 40.5 million
Large chains	7	$1,149.5 million
TOTAL	16	$ 525.6 million

SOURCE: Retailer questionnaire.

FIGURE 9-A

COMPARISON OF LATEST PERIOD OPERATING MARGINS
FOR FOOD RETAILERS



SOURCE: Retailer Questionnaire

FINANCIAL STATISTICS

The consultants summarized the retailers' financial statistics in Table 9-C. The figures reported are for 1) fiscal years ending during 1977, and 2) the average of three fiscal years ending during 1975, 1976 and 1977.

The term "gross margin," as used in this table, represents the difference between sales revenue and the cost of sales expressed as a percentage of sales.

The major conclusion to be drawn from this table is that there is no significant difference in the figures between large and small retailers.

The trend within the last three years indicates no major change in gross or net margin. The return on equity appears to have improved within the last financial period.

Included in Table 9-C is data extracted from the federal Anti-Inflation Board survey of retailers compiled in 1978. The Board's figures on after-tax net margins are substantially similar to the findings of this Commission's consultants.

DISCOUNTS, REBATES AND ALLOWANCES RECEIVED BY RETAILERS

The majority of the responses to the consultants' questionnaire were initially reported without off-invoice allowances. The consultants were not satisfied with these reponses and, after considerable consultation with the

TABLE 9-C

SUMMARY OF RETAILER FINANCIAL STATISTICS
(Fiscal Year Ends During 1977)

	Small Chains	Large Chains	Average	Significant Difference 95% Confidence Level
A. Latest Period				
Gross Margin	21.1%	20.0%	20.9%	no
Net Margin (after tax)	0.9%	1.1%	1.0%	no
Return on Equity (after tax)	18.3%	16.1%	17.1%	no
B. Latest 3 Period Average				
Gross Margin	20.3%	19.3%	20.1%	no
Net Margin (after tax)	1.0%	1.0%	1.0%	no
Return on Equity (after tax)	14.7%	14.3%	14.5%	no

Anti-Inflation Board Survey of Retailers

	Net Margin (after 50% tax)	Return on Equity (after 50% tax)
1975	1.10%	12.20%
1976	0.70%	9.15%
1977	0.85%	10.45%

NOTE: These figures include all off-invoice allowances.

SOURCE: Retailer questionnaire and *A Study of Profit Margins in the Food Industry*, Anti-Inflation Board (Ottawa, 1978).

retailers, obtained estimates of the off-invoice allowances from them.

Most of the retailer evidence at the hearing expressed the levels of rebates on the following basis:

(a) as a percentage of retail sales; and

(b) not including off-invoice allowances.

The tables prepared by the consultants on levels of rebates in this chapter (Tables 9-D and 9-E) express the rebate levels:

(a) as a percentage of retail purchases; and

(b) including estimated off-invoice allowances.

This method reflects greater accuracy and allows comparison with the processors' rebate levels reported as a percentage of processors' sales.

The consultants in Table 9-D reported the average rebate level for each food product category. These levels are calculated as the ratio of rebates received to purchases from the suppliers. The averages calculated include estimates of off-invoice amounts. As explained in Chapter 2, off-invoice amounts have to be estimated as the retailers do not itemize separately off-invoice amounts in their books of account.

Table 9-D indicates that the large chains receive significantly higher rebates for beverages, canned fruit, canned vegetables, cereal and frozen food when compared to the rebates received by small chains for the same products. However, the differences were not significant for other

TABLE 9-D

SUMMARY OF REBATES RECEIVED BY RETAILERS

Food Product	Small Chains	Large Chains	Average	Significant Difference 95% Confidence Level
Baked Goods	6.1%	9.4%	7.6%	NO
Beverages	1.3%	5.3%	3.0%	YES
Canned Fruit	1.4%	8.4%	4.7%	YES
Canned Vegetables	1.0%	9.1%	5.0%	YES
Cereal	1.3%	5.0%	2.9%	YES
Dairy Products	17.5%	25.0%	20.8%	NO
Fresh Produce	0.4%	2.4%	1.4%	NO
Frozen Food	0.6%	3.8%	2.1%	YES
Meat	1.8%	3.5%	2.5%	NO
Soup	1.9%	4.1%	2.9%	NO
Simple Average	3.2%	7.5%	5.1%	YES
Weighted Average (see Table 9-E)	7.4%	7.7%	7.5%	NO

NOTE: These figures include all off-invoice allowances.

SOURCE: Retailer questionnaire.

TABLE 9-E

RELATIVE IMPORTANCE OF SALES BY RETAILERS

Food Product	Grocery Stores		Combination Stores	
	Sale %	Relative Weight	Sale %	Relative Weight
Baked Goods	6.3%	11.8%	3.9%	5.4%
Beverages	11.1%	20.7%	2.8%	3.9%
Canned Fruit	2.2%	4.1%	5.3%	7.4%
Canned Vegetables	2.2%	4.1%	5.3%	7.4%
Cereal	1.3%	2.4%	1.4%	2.0%
Dairy Products	18.6%	34.8%	10.3%	14.4%
Fresh Produce	1.7%	3.2%	8.5%	11.9%
Frozen Food	5.4%	10.1%	6.6%	9.2%
Meat	2.5%	4.7%	22.3%	31.0%
Soup	2.2%	4.1%	5.3%	7.4%
TOTAL	53.5%	100.0%	71.7%	100.0%

NOTE: 1. Statistics Canada figures for canned goods are reported in aggregate only (6.5% for grocery stores, 15.8% for combination stores). We assume that canned fruit, canned vegetables and soups each accounted for one third of the canned foods sales. Data for the small chains and independents are from the grocery stores columns and for the large retailer are from the combination stores columns. The data are for Ontario.

SOURCE: Statistics Canada, Retail Commodity Survey, 1974 (catalogue 63-526).

products. The rebates for dairy products are considerably higher than for other products, averaging 20.8% for all retailers. These rebates are considered in depth in Chapter 6.

In Chapter 5, the average rebate levels offered by processors are listed. The Inquiry consultants found they corresponded roughly to the figures provided by retailers. The consultants caution that comparisons should be treated carefully due to the problems of defining various categories of food products. For example, the "beverages" reported by retailers include some purchases of fruit juices, whereas the reports by processors relate mainly to soft drinks.

The simple arithmetic average of rebates for large and small chains on all ten food products was 5.1% of the amount of purchases. Small chains averaged 3.2% rebates to purchases while the large chains averaged 7.5% rebates to purchases. This may be said to represent a statistically significant difference.

To verify their findings on the rebate levels, the consultants performed another analysis. Because of the importance of their findings to my conclusions, I quote the report of this analysis in full:

> "A more accurate measure of the rebate level is an average weighted by the relative importance of each product group. We measured the relative importance of each product group by its approximate

percentage of sales. This information was obtained from the Statistics Canada Retail Commodity Survey, 1974 (catalogue 63-526) and is presented in Table [9-E]. Several sources in the grocery industry indicated that these figures correspond accurately to the product mixes in small and independent stores, but slightly less accurately to large chain retailers. Errors due to changing product mix will overstate the rebate level for the large retailers in particular. This overstatement does not affect the substance of our conclusions.

"We selected the Statistics Canada data for grocery stores to represent the small chain retailers in our sample. The data for combination stores (grocery stores with fresh meat) were used for the large chains. These two different sets of weights help reflect the difference in the sales mix between the small chains group and the large chains. The weights that we used were figures adjusted to 100% for the 10 product groups. Their weighting to 100% allows direct comparison of the rebates of the major product groups in the various types of stores. It must be borne in mind that we have excluded non-food products from these calculations.

"The weighted average rebate level for the small chains was 7.4%. For the large chains the rebate level was 7.7%. These two averages were not

significantly different. It is important to note that the average rebate levels reported by processors on their sales and retailers on their purchases are similar. Differences can be attributed to the different weights of products in each sample and also to the fact that retailers have estimated the amount of off-invoice allowances they receive.

"The main reason for the similar rebate levels is the importance of dairy products. For the small retailer the sale of dairy products represents a significant proportion of his business. For the large chain, although the over-all sales volume is high, dairy products are relatively less important when considering the over-all sales mix. Thus the high rebate levels for dairy products (approximately 20.8%) have their greatest effect in raising the average rebate level for the small chains and independent retailer.

"Another reason for the similar rebate levels between the two groups is the relatively greater importance of fresh produce and meat sales in the sales mix of the large retailers. These two product groups carry low average rebate levels, 1.4% and 2.5% respectively. This has the effect of lowering the average rebate level for the large chains relative to that for the small chains."

Having determined the rebate levels received by retailers, I will now consider whether rebates are passed through to the consumer or not. If so, how is this achieved? To answer these questions, the consultants investigated the retailers' accounting treatment of rebates.

There are two methods of pass-through used, one direct and the other indirect. Table 9-F shows as Method 1, the direct method, and as Method 2, the indirect method.

In general, retailers calculate their selling price on the basis of the cost of goods plus a markup. The size of the markup is calculated partly by the amount of the selling, general and administrative expenses which must be defrayed. There are also many other factors to consider such as competitors' prices, the demand for the product and the availability of the product. The size of the markup will also vary according to the accounting method used, to the degree that the markup is based on defraying expenses.

The indirect method of pass-through, Method 2 in Table 9-F, shows a retailer who has chosen to apply rebates received against selling, general and administrative expenses in the amount of two units, leaving 20 units to be defrayed by markup ("units" represent dollars or multiples of dollars). Method 1 in the same table shows a retailer who has chosen to apply rebates received against the cost of goods sold in the same amount of two units, leaving 22

TABLE 9-F

RETAILER ACCOUNTING TREATMENT OF REBATES

Method 1: Direct			Method 2: Indirect		
Revenue		100	Revenue		100
Gross Cost of Goods Sold	78		Cost of Goods Sold		78
Rebates Received	2				
Net Cost of Goods Sold		76			
Gross Profit		24	Gross Profit		22
Selling, General and Administrative Expense		22	Selling, General and Administrative Expense	22	
			Rebates Received	2	
			Net Expenses		20
Net Profit		2	Net Profit		2
Markup		24	Markup		22

units to be defrayed by markup. However, the markup proceeds from a lower cost of goods sold than in Method 2.

The example given in the table illustrates the point that no matter whether pass-through is direct or indirect, and no matter which accounting treatment is used, the net profit to the retailer is the same. The price of the food product to the consumer is also identical.

As I have stated before, retailers receive rebates from processors in basically two ways:

(a) by cheque, or

(b) by off-invoice allowances.

The practice of the grocery industry is to account for rebates as such only if they are received by cheque, as in Method 2. Those rebates received by a reduction of the invoiced amount ("off-invoice") are recorded, but only as the net invoice amount, as in Method 1. For example, if a retailer receives a reduction of $1 per case off the invoice value of $10 per case, he records the cost of goods as $9 per case and does not make a separate entry representing the amount of the reduction.

The major implication of this accounting practice is that when a retailer is asked for his over-all rebate level, he will reply with a figure for those rebates other than off-invoice allowances.

PROFILE OF AVERAGE CHAIN RETAILER'S OPERATIONS

Figure 9-B is a profile of the average operation of large and small chains for the year 1978. The consultants prepared this profile from data obtained from, and direct interviews with, the major food retailers.

Unless otherwise indicated, the following definitions apply to Figure 9-B and to subsequent Figures 9-C and 9-D. "Gross margin" is the difference between sales and cost of goods sold. The "cost of goods sold" includes store delivery costs, warehousing costs and inventory costs and all allowances received by off-invoice methods. "Net profit" is the after-tax, after-extraordinary-items margin. "Utility costs" include cost of heat, light and electricity. "Labour costs" are costs for all non-head office labour excluding benefits and taxes. "Occupancy costs" include rent, realty taxes and utility costs. "Rebates" include discounts, allowances and rebates that are received in forms of payment other than off-invoice. These include co-operative advertising allowances, some volume rebates and other similar rebates. It does not include off-invoice allowances, which are accounted for under "gross margin."

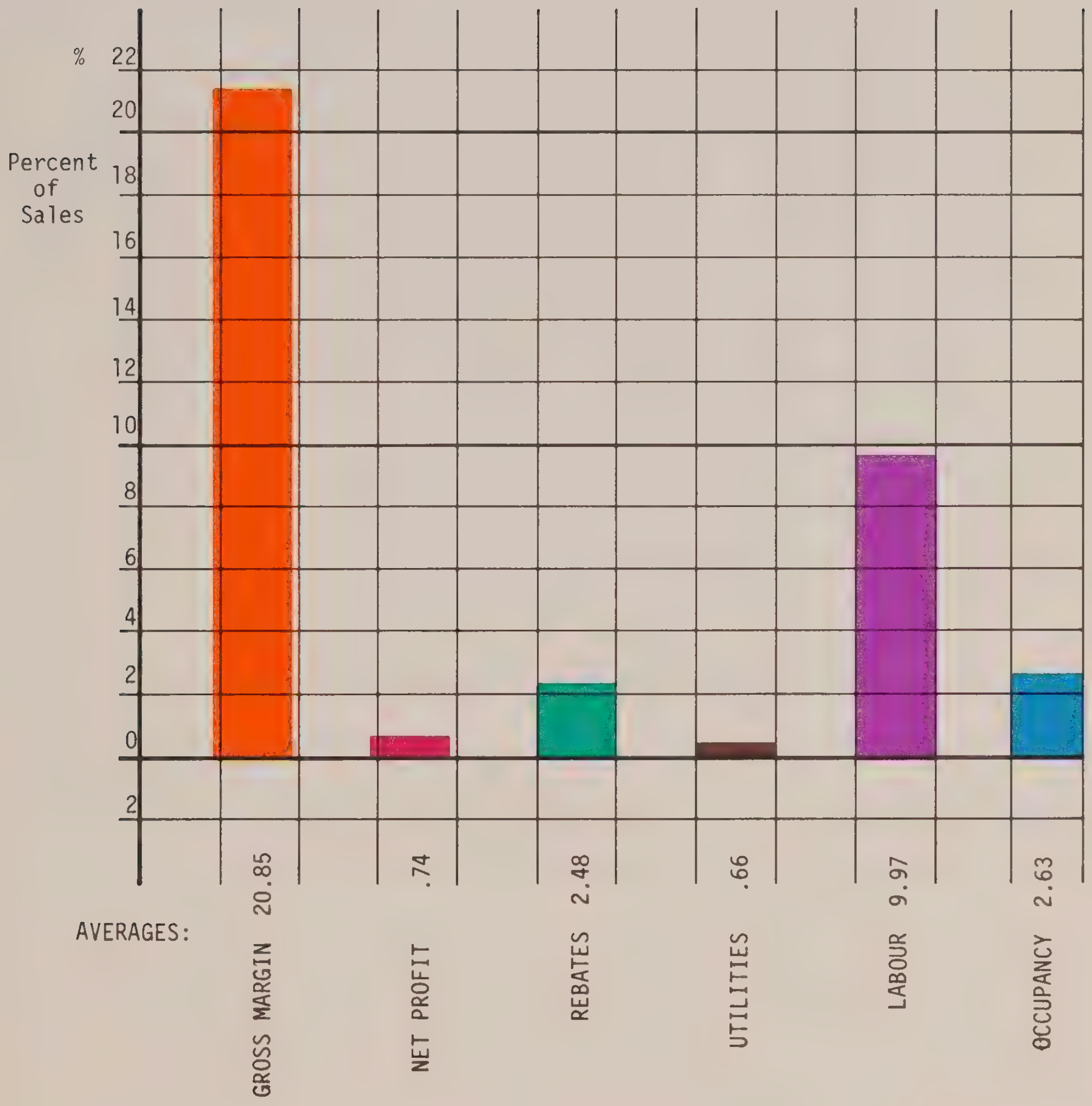
I wish to re-emphasize that "rebates" do not show off-invoice allowances, which are accounted for under "gross margin."

This profile is most significant in determining the effect of rebates on consumers, especially as summarized in (c) below.

FIGURE 9-B

PROFILE OF AVERAGE RETAILER OPERATIONS

1978



SOURCE: Corporate records

The significant conclusions from the figure are:

(a) Net profits average less than 1% of sales.

(b) Rebates represent 2.48% of sales.

(c) All factors remaining the same, if rebates paid by cheque alone were prohibited, the retailers would suffer a loss of 1.74% of sales. The only avenues open to avoid loss would be to buy cheaper from the supplier or to increase prices to the consumer.

(d) Net profits are less than one-third the size of rebates.

(e) Rebates average approximately one-fourth the level of labour costs, approximately the same as occupancy costs, and higher than both utility costs and net profits.

TOTAL AMOUNT OF REBATES

Our consultants reported that the average retailer received rebates by cheque in the amount of 2.48% of his sales. The retailers estimated that they received off-invoice allowances in the amount of 3.5% of their over-all sales. These figures were cross-checked against figures from the processor returns in response to the processor questionnaire.

It is my conclusion from the evidence and the investigations of the consultants, that the average total amount of rebates received by retailers approximates five to six

per cent of the retailers' sales. Further information on retailers' rebate levels can be found in Chapter 10.

TRENDS IN REBATES

Figures 9-C and 9-D show the trend of rebate payments, over the past five and eight years, relative to the other aspects of retailers' operations.

Again, the "rebates" illustrated include only rebates paid by cheque. Off-invoice allowances are accounted for in the "gross margin" projection.

Significant conclusions from these figures are:

(a) Both periods show a significant growth in rebates as a percentage of sales.

(b) Net profits have decreased significantly during the most recent five-year period.

(c) Gross margins have remained relatively constant over both the five- and eight-year periods. This fact, combined with declining net profits, indicates that retailers have experienced large increases in operating costs and overhead.

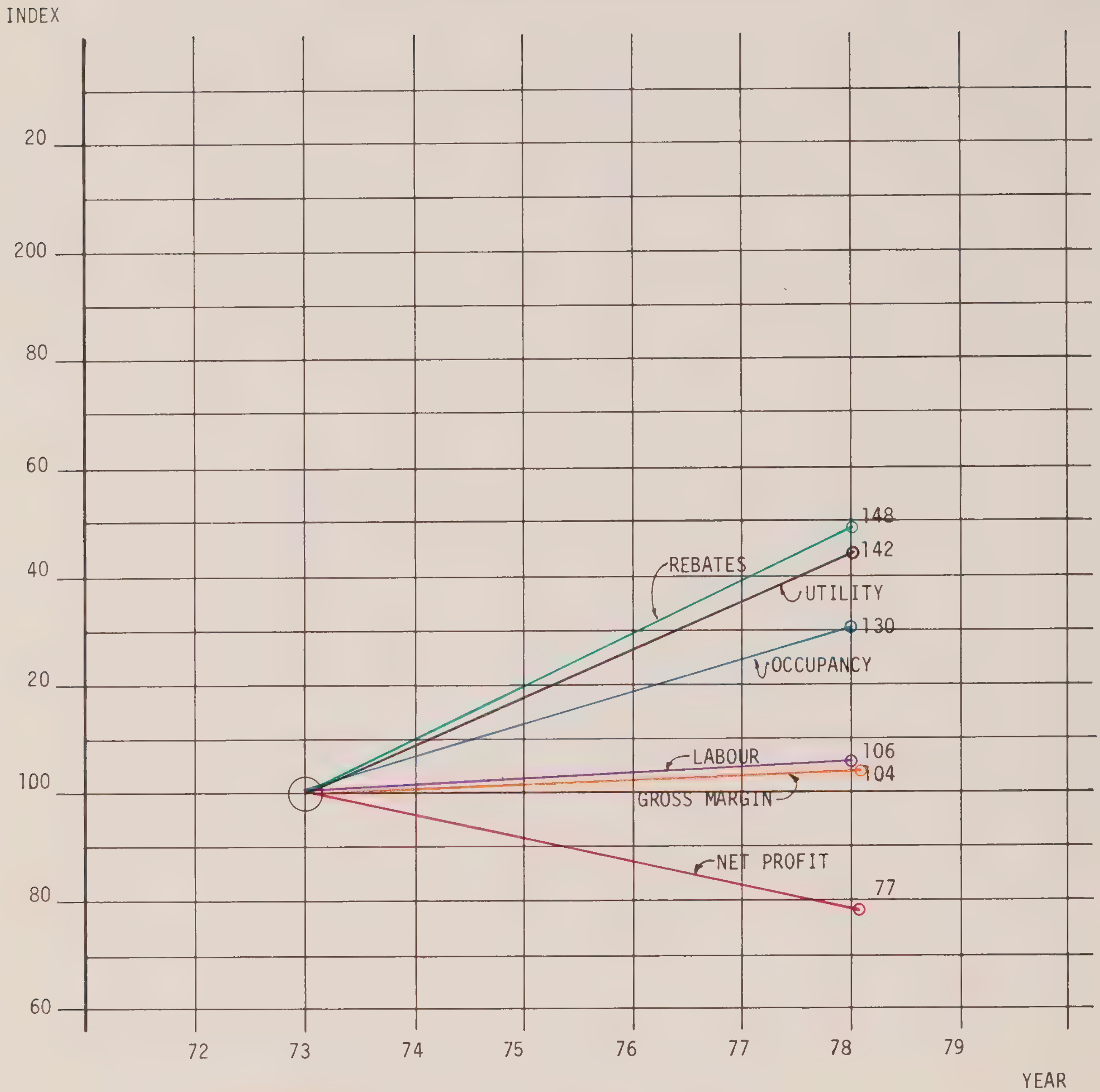
(d) Utility costs have grown significantly, particularly during the past five years.

(e) Labour costs have remained relatively constant as a percentage of sales.

From these figures, one can conclude that increased rebate levels have offset the increased costs experienced

FIGURE 9-C

COMPOUND GROWTH RATES, 5 YEARS

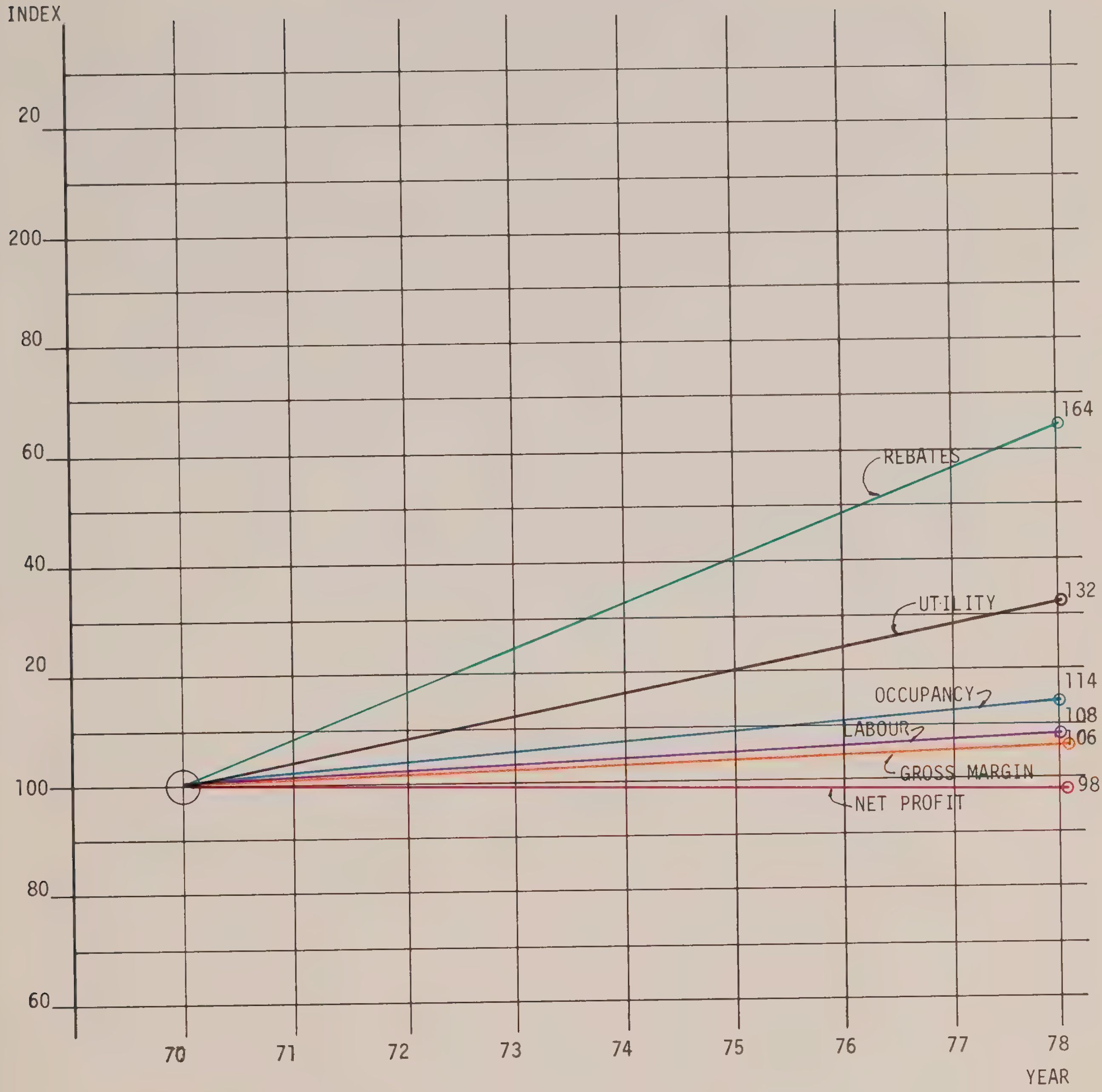


NET PROFIT - % OF SALES INDEXED.
GROSS MARGIN - % OF SALES INDEXED.
DISCOUNTS, ALLOWANCES & REBATES - % OF SALES INDEXED.
STORE LABOUR & FRINGE BENEFITS - % OF SALES INDEXED.
UTILITY COSTS - % OF SALES INDEXED.
OCCUPANCY COST - % OF SALES INDEXED.

SOURCE: Corporate records

FIGURE 9-D

COMPOUND GROWTH RATES, 8 YEARS



NET PROFIT - % OF SALES INDEXED
GROSS MARGIN - % OF SALES INDEXED
DISCOUNTS, ALLOWANCES & REBATES - % OF SALES INDEXED
STORE LABOUR & FRINGE BENEFITS - % OF SALES INDEXED
UTILITY COSTS - % OF SALES INDEXED
OCCUPANCY COST - % OF SALES INDEXED

SOURCE: Corporate records

by retailers and have helped them to maintain their margins of profit.

EVIDENCE CRITICAL OF REBATES RECEIVED BY LARGE RETAILERS

1. THE ONTARIO FEDERATION OF AGRICULTURE (O.F.A.)

The O.F.A. made an opening and closing submission to the Inquiry. In this chapter, I shall only deal with their submissions as they relate to large retailers and rebates. In his opening brief, Mr. Peter Hannam, President of the O.F.A., alleged that a few chain stores are using their market power to force up the prices their competitors have to pay for this merchandise and to force consumers to pay prices that they determine. This distorts the marketplace which harms farmers' access to consumers. "They do all this, just because it suits them," the O.F.A. claimed.

On the issue of retailer profits, the O.F.A. brief stated that it is not surprising that an industry with a high turnover of stock, little technology, and a relatively unskilled work force, has a low ratio of profits to sales. The O.F.A. argued that this did not lead to the assumption that low prices and efficiency prevail in the retail market. As for what price advantages the chains may exhibit over their smaller competitors, the O.F.A. alleged that "[a]ny price advantage a chain may have comes out of the hides of their [sic] competitors."

On the subject of competition between the large retailers, Mr. Hannam suggested there is ample evidence to

show that prices tend to follow those of the price leader and are not the result of true competition. According to him, "it is common knowledge" that the chains check the prices of their competitors regularly. "The competition in Ontario then would appear to be almost solely for market share, a conclusion which would support our opinion that we are dealing with an oligopolistic market."

2. GROCERY PRODUCTS MANUFACTURERS OF CANADA (G.P.M.C.)

The G.P.M.C. submitted an opening and closing brief to the Inquiry.

Its opening brief stated, under the heading of "Conclusions":

> "We have looked exhaustively at rebates, discounts and allowances in this submission and have declared our belief that when they are properly used and properly obtained, they are generally of benefit to the consumer, retailer and manufacturer. However, over the past ten years, a number of disturbing trends have arisen both in their use and in the methods by which they are exacted."

In its closing statement, the G.P.M.C. stated:

"At the end of the very extensive hearings, we remain convinced of two principal conclusions:

(i) the food industry in Ontario has been shown to be performing well and for the benefit of the consumer; and,

(ii) there is no firm basis in either the evidence before the Commission or any economic theory presented to the Commission in argument for believing that the performance of the industry would be improved for the benefit of consumers by new government rules or intervention."

3. CONSUMERS' ASSOCIATION OF CANADA (C.A.C.)

The C.A.C. is a voluntary, non-profit association with a national membership in excess of 100,000. Its brief expresses the concerns of Canadian consumers, not just those who reside in Ontario.

It is a well-reasoned brief and I will summarize this submission, as it relates to rebates and the retailer, as follows:

(a) Two largely opposing interpretations of the food industry's pricing system have been presented to the Inquiry:

(i) Large retailers submit that discounts are the outcome of fierce competition among themselves and suppliers. This competition

reduces retailers' costs and moderates the prices consumers pay for their groceries.

(ii) The farm community and suppliers argue that such pricing systems are discriminatory and are, for the most part, an outgrowth of the immense market power of the retailing chains. It is also alleged that such a pricing system has the effect of denying the benefits of competition to the consumer.

The C.A.C. concludes that the rebate system has both positive and negative effects for the efficiency of the industry and for consumers. In accordance with these perceptions, the C.A.C. recommends changes in The Combines Investigation Act to correct certain problems. This issue is considered in Chapter 16, Rebates and the Law.

4. ONTARIO LIBERAL PARTY

Dr. Stuart Smith, Leader of the Ontario Liberal Party, stated in evidence that the essence of free enterprise is competition. Concentration of economic power in the hands of relatively few buyers and sellers is the antithesis of competition. Dr. Smith submitted that he perceived a growing concentration in the Ontario food industry. The retail market, he said, has come to be dominated by three major chains in the last 25 years. These concerns are investigated in Chapter 13, Concentration and Rebates.

5. <u>DR. BRUCE MALLEN</u>

Dr. Mallen is an economist holding a Master of Business Administration Degree and a Doctor of Philosophy in the field of economics and marketing. His paper, <u>A Study of Supermarket Market Power</u>, deals with consumer/store interaction.

Dr. Mallen's report concluded that "there is no evidence that predatory trade practices are a cause of concentration." This report is also considered in Chapter 17, Findings of Other Inquiries and Studies.

He stated that the normal concern with oligopolies is that they will not allow or permit whatever efficiencies are created to be passed on to the consumer; therefore, prices should be higher in an oligopolistic situation. Typically, he stated, when a large retailer in an oligopolistic industry reduces the price of an item, other oligopolists will follow suit.

Dr. Mallen was not aware of any evidence that the degree of competition between major participants in the Ontario market is going to diminish.

Dr. Mallen's evidence, while of some assistance, was mainly theoretical. He was unable to provide the Inquiry with any facts pertaining to the effect of rebates in Ontario on prices to the consumer.

EVIDENCE SUPPORTIVE OF REBATES RECEIVED BY LARGE RETAILERS

1. STEINBERG INCORPORATED

Mr. Jack Levine, President, stated that all moneys received for discounts contribute to the effectiveness and efficiency of the corporate organization. If the company did not receive discounts, the gross margin (in this sense, meaning the markup applied in pricing) would have to increase. All rebates are passed through to the store-level price and are reflected in the corporation's profit and loss statement.

2. CANADA SAFEWAY LIMITED

Mr. Norman Fingler, Toronto Zone Manager for the corporation, testified that all rebates, except those requiring promotional performance, are credited to the cost of goods sold. Allowances requiring promotional performance contribute to the reduction of advertising expense.

3. LOBLAWS LIMITED

Mr. David Nichol, President, testified that off-case allowances are reflected in the corporation's gross margin.

Rebates received by Intersave, a buying group composed of Loblaws and affiliated companies, are remitted monthly to Loblaws.

In its closing brief, Loblaws submitted:

> "No evidence has been presented to the Commission that farmers, processors, or consumers are injured by discounts, allowances and rebates. In fact, the evidence recognizes and indicates that the cost of savings to food retailers generated by discounts, allowances and rebates encourage efficiency and are passed on to consumers in the form of lower prices."

4. DOMINION STORES LIMITED

Mr. Thomas G. Bolton, Chief Executive Officer of Dominion Stores, explained that Dominion Stores refers to discounts, allowances and rebates as "earned cost reductions" (abbreviated to "E.C.R.'s") in recognition of the corporation's view that retailers receive rebates in consideration for the benefits that a supplier derives from dealing with a customer like Dominion Stores.

To quote from the brief:

> "(a) E.C.R.'s are offered to us by suppliers and have to be earned by us. The nature of the service which we must perform to earn the cost reduction may be stipulated unilaterally by the supplier, as in the case of cash discounts and volume discounts, or negotiated for performance with us as in the case of promotional allowances.

(b) <u>All E.C.R.'s are taken into account in arriving at our actual cost for goods purchased by us</u>. This is the case for the purposes of our financial statements and for determining our actual cost of goods, net of all discounts and allowances.

(c) <u>E.C.R.'s are entirely legal</u>.

(d) <u>If all E.C.R.'s were discontinued, the prices paid by consumers would rise</u>...[O]ur net earnings are one cent on each dollar of sales. We are able to maintain the price levels in our stores and make that slender net return on sales only by keeping our costs as low as possible. This we do, in part, by earning reductions in the cost of the goods which we sell. If, for any reason, we were no longer able to earn these cost reductions, the increased cost of our goods would have to be passed on to the consumer."

5. OTHER LARGE RETAILERS

Officers from several other large retailers also testified at the Inquiry. They corroborated the evidence of the retailers above in most respects. They all submitted:

(a) that they earn the rebates they receive;

(b) that rebates enable retailers to reduce prices to consumers; and

(c) that, if rebates were discontinued, the price of food to the consumer would rise.

6. J. DONALD TIGERT

Mr. J. Donald Tigert is a financial analyst who has a specialized knowledge of the food industry in North America. His studies indicate that the food chains in Ontario report the lowest gross margins of any market in Canada and substantially lower gross margins than similar chains in United States. The food chains' pre-tax profit margins are also lower in Ontario than in any other region of Canada, and lower than in most parts of the United States. The witness expressed the opinion that the lower gross margins of the food chains in Eastern Canada, relative to those of the chains in Western Canada and in the United States, represent a savings of $140 million per year for food to consumers in Eastern Canada, and particularly in Ontario.

The food chains' return on equity is furthermore not as high as returns of non-food investments.

Mr. Tigert testified as to his opinion of the effect of rebates on consumers: "...I have to conclude [that] to the extent the [chains in Ontario] are getting rebate moneys, they are passing them along to the consumers in the form of lower prices." It was further his opinion that if rebates were discontinued, prices to the consumer would have to rise to compensate for this revenue since the chains in Ontario do not presently make an adequate profit margin.

Under cross-examination by the O.F.A., Mr. Tigert expressed his view as to the competition in the Ontario retail food market. He testified that Ontario retailers demonstrate high sales per square foot and low profit, two trademarks of efficient performance. The reason for this efficient performance, in Mr. Tigert's view, is intense competition at the retail level.

7. RETAIL COUNCIL OF CANADA

The Retail Council supported the view that consumers benefit from rebates paid to retailers. The Council expressed its conviction that the Ontario market is strongly competitive. This competition ensures, in the Council's opinion, that whatever immediate economic advantage accrues to vendors from a discounting system is passed through to the consumer.

The brief further submits that the Canadian retail stores are more efficient than their counterparts in the United States. This fact would tend to indicate that rebates do not adversely affect this aspect of the business. Since neither inefficiency nor profiteering is occurring in the food chain, the only conclusion possible is that rebates are passed on to the consumer in the form of lower prices, states the brief.

The Council is finally of the view that there is a direct relationship between the high level of efficiency within the food industry and the application of many

beneficial management practices such as are embodied in the rebate system.

CONCLUSIONS

The following summarizes my conclusions on the evidence examined in this chapter:

1. The retail segment of the food industry is moderately to highly concentrated. It is estimated that the retail food chains, including convenience store chains, account for 73% of food sales in Ontario.

2. There is no significant difference in the cost of sales and profit levels between large and small chains.

3. Net profits (after tax) for large and small chains average 1% of sales. The return on equity (after tax) for small chains amounts to 18.3% compared to 16.1% for large chains.

4. All rebates, whether received by cheque or by off-invoice allowance, are reflected in the net profit figures of retailers.

5. Rebates are a major source of revenue to the retail chains. Rebates received by cheque amount to 2.48% of retailer sales. Off-invoice allowances approximate 3.5% of retailer sales.

Therefore, all rebates received by retailers approximate 6% of sales.

6. Rebate levels have increased substantially in the past eight years.

7. The weighted average rebate level for small chains is 7.4%, and for large chains, 7.7%, of purchases.

8. The conclusions above indicate that chains receive approximately 6% of sales in rebates and achieve a profit of 1% of sales. The consultants' reports on retailer accounting systems show that rebates either lower the net cost of goods to retailers or lower the net costs of retailer operations, both of which in turn lower the cost of goods to consumers. This conclusion, namely that rebates are used to lower the prices that consumers pay, is reinforced by the fact that the average return on equity (after tax) by the chains is 17.1%. This is, at best, an average rate of return when compared with non-food industries.

9. If rebating were to be disallowed, it would probably result in consumers' paying higher prices for food.

10. The evidence at the Inquiry indicated that there is a real and intense competition between the chains for market share. Volume turnover is the

key to success when operating on a small profit margin. The chain buyers reflect this competition and endeavour to buy as cheaply as they can. In setting sale prices for food, the chains are attentive to the prices of competitors, and a major motivation is to increase sales so as to increase their market share.

11. The evidence indicated that Ontario retail chains operate more efficiently, as a whole, than other food chains in North America. This is reflected in the fact that Ontario food prices are the lowest in Canada.

CHAPTER 10

SMALL RETAILERS AND REBATES

GENERAL

It was alleged during this Inquiry that large retailers received higher rebates than smaller retailers and that consequently, the latter are disadvantaged in their efforts to compete on a price basis. This view is expressed in the brief of the Ontario Federation of Agriculture:

> "Discounts to the larger chains mean that they buy cheaper than their competitors. They can do this because they have a virtual stranglehold on the consumer market....
>
> "If this trend toward higher rebates is allowed to continue, the independent grocer will be less and less able to show a profit."

Mr. Kenneth Gadd, the General Manager of the Canadian Federation of Retail Grocers, submitted a brief which expresses similar concern:

> "My greatest concern is consolidation of control in the distribution of food in Ontario into relatively few hands."

The brief proceeds to emphasize the deteriorating status of the independent grocer in Ontario.

Unfortunately, only two owners of independent retail stores came forward to testify before the Inquiry despite the wide publicity the hearings were given.

Mr. William James Hill owns and operates Lakeshore Marketeria located in Bronte, Ontario. His store contains approximately 7,000 square feet and carries a full line of groceries. Mr. Hill has been in business for more than 30 years despite the fact that fifteen chain stores operate within five miles of his store. He testified that he is able to match or undersell the prices offered by his chain rivals. In fact, he testified that he had no complaints about supermarket competition and that he is able to attract customers by providing services which chain supermarkets are unable to provide.

Mr. Carl Quaranto operates an independent retail store of eight to nine thousand square feet, in Fenelon Falls. His main competition is an IGA outlet but in Lindsay, which is 17 miles from Fenelon Falls, are located three chain outlets -- Dominion, Loblaws and A&P. Mr. Quaranto must compete with all these stores.

This witness testified that his prices on national brands are as low as or lower than the chains; Mr. Quaranto buys from the wholesaler National Grocers. He is also able to provide personalized service which the chains cannot provide. His only complaint about the chains is their loss-leader selling.

From the results of their original survey, the consultants testified that small retailers receive approximately the same magnitude of rebates that large retailers receive. This is mainly due to the fact that small retailers purchase from large wholesalers which purchase in volumes comparable to those purchased by the large retailers.

Due to the lack of evidence on this issue, I asked the consultants to conduct a more intensive survey of small retailers in order to verify their original conclusions. The results are reported below in the section entitled, "Small Retailers' Rebate Levels."

As elsewhere in this report, much of what is stated here will be restated in other chapters, particularly in Chapter 13, Concentration and Rebates. I realize this may make my Report somewhat repetitious but, on the other hand, I believe that such repetition is necessary to maintain each chapter as a complete unit rather than to burden the reader with tiresome references. It may also assist the reader in understanding very complex topics and concepts.

DEFINITIONS OF TYPES OF SMALL RETAILERS

Who are the small retailers of Ontario? Retailers themselves may be divided on the question of whether or not they are chain retailers.

Throughout this report, I have used the Statistics Canada definition of "chain" which is a group of four or more stores under common ownership. I have subdivided the

category of chain retailer into major and minor chains. The major chains in Ontario are the six large retailers - Dominion Stores, Loblaws, Steinberg/Miracle Food Mart, A&P, Oshawa/Food City and Safeway. The minor chains are more regional operations, for example, Knob Hill Farms and Calbeck's. The minor chains are large, however, in comparison to single-store grocery operations. Accordingly, it is difficult to achieve a commonly accepted definition for the term "small retailer."

A further distinction between types of retail stores is the Statistics Canada classifications of "combination" and "grocery" stores. A "combination store" has at least 20% of its sales in fresh meat, while a "grocery store" has less than 20% of its sales in fresh meat. The term "combination" thus expresses the combination of a store's grocery and meat operations. A typical combination store is any of the stores of the large chains. A typical grocery store may be either a large grocery store selling little fresh meat or what is commonly called a convenience store with a full line of groceries excepting fresh meat.

The definition of "independent retailer" used in this report is that of a retailer who does not satisfy the Statistics Canada definition of a "chain." Therefore, an "independent retailer" is one owning three retail outlets or less. Quite often, independents have only one store.

The following is a list of the various types of small retailers in Ontario:

(1) minor combination chains,

(2) major and minor convenience chains,

(3) franchised and voluntary group independents,

(4) unaffiliated combination independents,

(5) unaffiliated convenience independents,

(6) specialty chains, and

(7) specialty independents.

These terms will be explained as I describe the types.

1. Minor Combination Chains

The first type within this group is the minor combination chain. Minor chains such as Knob Hill Farms (five stores) and Calbeck's (six stores) differ from the major chains in that the minor chain's stores are generally located in a region rather than province-wide and in that they are not vertically integrated* to a significant degree. The minor chains are like the major chains in that they purchase most, if not all, of their merchandise directly from suppliers. However, most, if not all, minor chains are members of buying groups, whereas only three of the six major chains (Loblaws, A&P and Oshawa/Food City) are members of such groups. The minor combination chain usually has as much selling space in each store as the major combination chain and sells the same full line of commodities.

* This term is explained more fully in Chapter 12. It is sufficient to explain it, here, as connoting an affiliation at another level of the food chain. For example, the Becker Company is a vertically integrated chain in that the retail outlets are supplied with milk from the company dairy.

2. Major and Minor Convenience Chains

The second type within this group is the major and minor convenience store chains. This store also may be operated on a franchise basis but not always: Mac's Convenience Stores Limited, for example, franchises its stores, while the Becker Company owns most of its stores. The convenience stores range in size from 600 to 2,400 square feet and carry a limited line of products, usually eliminating fresh meat but concentrating on tobacco products and milk.

These stores are called "convenience" stores because they generally offer consumers proximity, later hours on week nights and week-ends, and shorter lineups; these are privileges for which the consumer must often pay a premium in the form of higher prices. In addition to the major chains of Mac's and Becker's, Ontario has many convenience store chains whose sales are less important, among which are Pinto Stores (an M. Loeb franchise), Seven-Eleven (a chain based in the United States), and Jug City (an Oshawa Group franchise).

3. Franchised and Voluntary Group Independents

The third type within this group is the franchised and voluntary group independents. As explained in the wholesaler section, the franchised independent, often franchised to one of Ontario's three largest wholesalers, resembles the independent in that the franchised store owner invests his own funds and retains whatever profits the store earns. However, the sales of these independents are often

represented as the sales of a chain (see Table 10-B), or as the sales of the wholesaler (see Table 10-C). This classification reflects the close resemblance which a franchisee bears to the chains in that the franchisee usually must sell the franchisor's products at a price established by the franchisor, and adhere to the franchisor's merchandising policies. The independent who is a member of a voluntary group is related to his wholesaler in much the same way as the franchisee, as explained in Chapter 8, Wholesalers and Rebates.

4. Unaffiliated Combination Independent

The fourth type of small retailer is the unaffiliated combination independent. The unaffiliated independent may deal directly with some suppliers, but he buys most dry groceries -- including breakfast cereals, canned and frozen fruits and vegetables, biscuits and many other items -- from wholesalers. The unaffiliated independent may buy from several wholesalers; in major metropolitan areas like Toronto and Hamilton the independent's choice of wholesaler is wide. The wholesaler patronized by the unaffiliated independent often belongs to a buying group.

5. Unaffiliated Convenience Independent

The fifth type within this group is the unaffiliated convenience independent. This independent's store usually measures less than 7,000 square feet and is often referred to as the "ma-pa" store, reflecting the fact that such stores are often family owned and family operated. These

stores are also frequently referred to as "corner stores" reflecting their location, but it should be noted that this term may refer as well to the chain convenience store. However, the chain convenience store often has the advantage of connection with a dairy, as in the case of Mac's and Becker's, for instance, or with a wholesaler, as in the case of the Pinto and Jug City stores.

6. and 7. Specialty Chains and Specialty Independents

Yet another type within the group is the specialty store: the local butcher and baker as well as the local fruit and vegetable grocer are examples. These stores, too, may be organized into chains which have diversified into products other than the specialty. Ziggy's is an example of a specialty chain specializing in meat products which also happens to be affiliated with Loblaws Limited and the Weston empire.

SMALL RETAILERS' MARKET SHARES

Table 10-A is a breakdown of retailers by type of retailer showing store numbers for each type. It is interesting to note that there are at least 7,702 stores in Ontario which are classified under the general heading of "small retailer", while there are only 689 stores which are classified under the heading "large retailer".

Table 10-B shows the breakdown of sales for large retailers compared with small retailers. This table, presented to the Commission by stock analyst J. Donald Tigert,

TABLE 10-A

TYPES OF RETAILERS AND NUMBER OF STORES IN ONTARIO, 1979

Type of Retailer	Number of Chains	Number of Stores
A. Major Combination Chains	6	689
B. Minor Combination Chains	6	38
C. Major and Minor Convenience Chains (including franchised stores)	18	2,036
D. Franchised and Voluntary Group Combination Chains	14	902
E. Unaffiliated Combination and Convenience (Grocery) Stores		4,726

SOURCE: Canadian Grocer, August, 1979.

TABLE 10-B

DISTRIBUTION OF ONTARIO FOOD SALES 1974 - 1978

Combination Stores (1)	1974	1975	1976	1977	1978
Chains	$2,642	$3,072	$3,370	$3,710	$4,193
Independents	688	800	871	920	1,041
Total	$3,330	$3,872	$4,241	$4,630	$5,234
Grocery & Confectionery Stores (2)					
Chains	186	232	248	274	312
Independents	403	474	624	599	618
Total	589	706	872	873	930
All Other Food Stores(3)					
Chains	64	55	59	61	65
Independents	338	353	407	376	415
Total	402	408	466	437	480
Total Market					
Chains	2,892	3,359	3,677	4,045	4,570
Independents	1,429	1,627	1,902	1,895	2,074
Total	4,321	4,986	5,579	5,940	6,644
Market Shares					
Combination Chains	61.1%	61.6%	60.4%	62.5%	63.1%
Combination Independent	15.9	16.0	15.6	15.5	15.7
Other Chains	5.8	5.8	5.5	5.6	5.7
Other Independent	17.2	16.6	18.5	16.4	15.5
Total Market	100.0%	100.0%	100.0%	100.0%	100.0%

NOTE: 1. Combination Stores - grocery stores with 20% or more fresh meat (includes supermarkets of the type operated by Dominion, Loblaws, Miracle Mart, IGA and Knob Hill Farms).

TABLE 10-B

DISTRIBUTION OF ONTARIO FOOD SALES 1974 - 1978
(continued)

NOTE: 2. Grocery, confectionery & sundries store - grocery stores with 20% or less fresh meat (includes "jug milk" and "convenience" stores of the type operated by Becker's and Mac's Milk.

3. All other food stores - bakery product stores; candy, nut and confectionery stores; dairy product stores; egg and poultry stores; fruit and vegetable stores; meat markets; fish markets; delicatessen stores (includes stores such as Bittner's, Fruit Fair, Laura Secord, Woman's Bakery).

SOURCE: Retail Trade in Canada, Catalogue No. 63-005, Statistics Canada submitted by J. Donald Tigert.

indicates that sales of combination chain stores are about four times greater than sales of independent combination stores. The combination chains referred to by Mr. Tigert in this table include major combination chains like Dominion, minor combination chains like Knob Hill, and franchised and voluntary group combination chains like I.G.A. Table 10-A and Table 10-B together show that the majority of stores are small retailer stores but that the majority of sales come from large retailer stores.

Table 10-C shows market shares over the eleven-year period 1969 to 1979. The market share of the two groups -- group independents and unaffiliated independents -- shows a sharp decline in the first six years of that period and a slow decline in the last five years. This trend is treated more fully in Chapter 13 on concentration.

The next section of this Chapter treats the question: "Are large retailers increasing their market share by receiving larger rebates than smaller retailers?"

SMALL RETAILERS' REBATE LEVELS

This section considers rebate levels for small retailers. In order to examine this issue, I instructed the consultants, Laventhol and Horwath, to expand their original questionnaire analysis so that it would include retailers smaller than the "small chains" initially surveyed. The Commission was originally satisfied that the consultant's methods and conclusions were soundly established. However, the Ontario Federation of Agriculture persistently

TABLE 10-C

DISTRIBUTION OF ONTARIO FOOD SALES, 1969 - 1979

		Total Independents	
	Chains' Share	Group Independents	Unaffiliated Independents
1969	61.2%	23.1%	15.7%
1970	63.1	21.4	15.5
1971	64.4	19.7	15.9
1972	69.8	15.8	14.4
1973	70.7	16.8	12.5
1974	72.2	17.6	10.2
1975	72.2	17.7	10.1
1976	70.8	18.5	10.7
1977	72.4	17.6	10.0
1978	73.1	17.2	9.7
1979	73.8	16.8	9.4

SOURCE: Canadian Grocer, February, 1980.

questioned and criticized Laventhol and Horwath's work. The Federation's questions came both during the hearings and after the hearings in public forums. While the Commission is of the opinion that none of the arguments put forth by the O.F.A. discredits the consultant's work, in order to thoroughly treat all questions raised, the additional data reported below was collected and processed.

In their original surveys, the consultants found that small retailers' rebate levels are closely related to the rebate levels of the wholesalers through which the small retailer buys. The consultants' evidence is that the rebates received by wholesalers are of the same level as rebates received by retail chain stores which buy directly from suppliers.

Ten small retailers, operators of single stores throughout Ontario, were asked to respond to the original retailer questionnaire. All of these retailers offer to consumers a combination store's product mix, meaning a full line of groceries. Furthermore, meat sales account for not less than 20% of sales. The average sales of these small retailers is $3.7 million with sales ranging from less than $.5 million to $13 million.

In order to assure a proper sample for the survey of the small retailer, the group of small retailers was divided into two subdivisions based on common ownership characteristics. One subdivision consisted of stores within what are called "franchised and voluntary group combination chains" and the other subdivision consisted of stores

called "unaffiliated combination independents," as defined previously. The stores within both subdivisions were selected on a random basis.

The analysis of this data will deal with two questions:

1. What are the differences and similarities in rebates between different types of retail operations (combination chain versus independent combination store versus convenience chain)?
2. What are the differences and similarities in rebates between different sizes of retail operations (chain versus non-chain combination store)?

Table 10-D presents financial returns for the entire sample including all large and small retailers sampled. The upper portion of the chart compares the gross margin, net margin after tax and the return on equity of combination chain stores with all other combination stores surveyed. The significant findings from this Table are represented in the third and ninth rows. These figures indicate that there is no statistically significant difference in the gross margin, net margin after tax, or return on equity between the large and small combination retailers sampled.

Furthermore, there is no statistically significant difference in the returns of the various types of retailers when compared with each other. In other words, while the actual averages of the samples appear different, the financial characteristics of all operations are not

TABLE 10-D

RETAILER FINANCIAL STATISTICS

(Fiscal 1977)

(all figures are percentages)

	Gross Margin	Net Margin (after tax)	Return on Equity
Large Combination chain retailers	19.9	1.0	17.2
Small Combination Retailers	15.5	1.6	24.2
Significant difference at 95% confidence level	NO	NO	NO
Large Combination Chains	20.0	1.1	16.1
Small Combination Chains	19.8	0.7	19.8
Convenience Store Chains	22.0	1.0	16.7
Small Unaffiliated Combination Store	14.7	1.3	22.0
Franchised and Voluntary Group Stores	18.2	2.2	35.6
Significant difference at 95% confidence level	NO	NO	NO

SOURCE: Retailer questionnaire.

significantly different when the results are analyzed to reflect the limitations of the sample. The small sponsored retailers' return on equity figure (35.6%) should be treated with caution because several retailers warned that the value of their investment in land and buildings is substantially understated. The understatement is caused by the fact that these values often represent an investment made in the past and consequently, the values do not reflect current values. This understatement has the effect of raising the small sponsored retailer's return on equity above what it would otherwise be.

The consultants proceed to analyze rebates in three different ways. First, they compared the rebate levels of retailers classified according to type. Second, they compared the rebate levels of the combination retailers classified as either chain retailer or franchised and unaffiliated retailer. Third, they related the rebate levels to the size of all firms regardless of classification. These analyses are set out below.

1. Table 10-E presents the first analysis, comparing the rebate levels of retailers classified according to type. The bottom row of the table gives the weighted average of the rebates according to the retailer's sales mix. The most important conclusion to be drawn from this table is suggested in the last row which shows that the weighted average rebate levels are not significantly different when comparing one type of retailer to another. The answer to the first question above, then, is: no, there is no significant difference in rebate levels between different types

ANALYSIS OF REBATES RECEIVED BY RETAILERS

Food Product	Major Combination Chains	Minor Combination Chains	Major and Minor Grocery Convenience Chains	Unaffiliated Combination Independents	Franchised and Voluntary Group Combination Independents	Average	Significant Difference 95% Confidence
Baked Goods	9.4%	2.4%	8.0%	8.6%	11.6%	8.3%	NO
Beverages	5.3%	0.5%	1.7%	8.1%	5.1%	4.6%	YES
Canned Fruit	8.4%	2.2%	0.9%	11.2%	10.2%	7.2%	YES
Canned Vegetables	9.1%	1.1%	0.9%	11.7%	8.6%	7.4%	YES
Cereal	5.0%	1.9%	0.9%	8.5%	4.9%	4.8%	YES
Dairy Products	25.0%	26.1%	13.3%	18.6%	27.4%	21.0%	YES
Fresh Produce	2.4%	0.0%	0.7%	0.5%	4.5%	1.5%	YES
Frozen Food	3.8%	1.3%	0.9%	5.3%	2.9%	3.1%	YES
Meat	3.5%	0.6%	2.4%	6.4%	5.8%	4.0%	NO
Soup	4.1%	3.5%	0.9%	4.6%	3.1%	3.4%	NO
Weighted Average	7.7%	4.6%	6.3%	8.2%	9.1%	7.3%	NO

NOTE: The following groups have a combination store sales mix -- Large Chains, Small Combination Chains, Small Independents, Small Sponsored -- and are weighted accordingly. The Convenience Chains group have a grocery store sales mix, and are weighted accordingly.

SOURCE: Retailer questionnaire.

of retailers. This answer is amplified below under the heading "Factors Affecting Rebate Levels".

The weights used for weighting rebate levels by sales mix are from Statistics Canada Retail Commodity Survey, 1974 (catalogue 63-526), and are reprinted here as Table 10-G. These are the same figures used to weight the rebate levels in Chapter 9, Large Retailers, Consumers and Rebates.

The conclusion reached by this analysis is identical to the conclusion reached by the consultants in their Brief Analysis, presented publicly at the Inquiry hearings.

2. Table 10-F presents the second analysis, comparing the rebate levels of combination retailers classified according to ownership. The group of chain combination retailers includes both major and minor combination chains. Examples of such retailers are the familiar large chains like Loblaws and Dominion, and smaller chains like Knob Hill and Calbeck's. The group of franchised and unaffiliated combination retailers includes independent combination stores and members of franchised and voluntary groups like I.G.A. or Red & White. The question that is addressed in this comparison is, "Do different forms of retail ownership affect rebate levels?"

Table 10-F shows that the total weighted average of rebates received by all combination retailers is 7.6%. There is no significant difference in the rebate level of the two groups of combination retailers. Thus, the answer

TABLE 10-F

ANALYSIS OF REBATE LEVELS BY SCALE OF RETAILER OPERATIONS

Food Product	Chain Combination Retailer	Franchised and Unaffiliated Combination Retailers	Average	Significant Difference 95% Confidence
Baked Goods	7.3%	9.5%	8.4%	NO
Beverages	3.8%	7.2%	5.5%	YES
Canned Fruit	6.5%	10.9%	8.7%	YES
Canned Vegetables	7.3%	10.7%	9.1%	NO
Cereal	4.0%	7.4%	5.8%	YES
Dairy Products	25.3%	21.2%	23.3%	NO
Fresh Produce	1.7%	1.7%	1.7%	NO
Frozen Food	3.0%	4.6%	3.8%	NO
Meat	2.6%	6.2%	4.4%	YES
Soup	3.9%	4.2%	4.0%	NO
Weighted Average	6.8%	8.5%	7.6%	NO

NOTE: 1. Chain retailers have 4 or more stores; franchised and unaffiliated combination retailers have less than 4 stores.

2. All retailers in this table have a combination stores sales mix, and are weighted accordingly.

SOURCE: Retailer questionnaire.

TABLE 10-G

RELATIVE IMPORTANCE OF SALES BY RETAILERS

(% of total sales)

Food Product	Grocery Stores		Combination Stores	
	Sale %	Relative Weight	Sale %	Relative Weight
Baked Goods	6.3%	11.8%	3.9%	5.4%
Beverages	11.1%	20.7%	2.8%	3.9%
Canned Fruit	2.2%	4.1%	5.3%	7.4%
Canned Vegetables	2.2%	4.1%	5.3%	7.4%
Cereal	1.3%	2.4%	1.4%	2.0%
Dairy Products	18.6%	34.8%	10.3%	14.4%
Fresh Produce	1.7%	3.2%	8.5%	11.9%
Frozen Food	5.4%	10.1%	6.6%	9.2%
Meat	2.5%	4.7%	22.3%	31.0%
Soup	2.2%	4.1%	5.3%	7.4%
TOTAL	53.5%	100.0%	71.7%	100.0%

NOTE: 1. Statistics Canada figures for canned goods are reported in aggregate only (6.5% for grocery stores, 15.8% for combination stores). We assume that canned fruit, canned vegetables and soups each accounted for one third of the canned foods sales. Data for the small chains and independents are from the grocery stores columns and for the large retailers are from the combination stores columns. The data are for Ontario.

SOURCE: Statistics Canada, Retail Commodity Survey, 1974 (catalogue no. 63-526).

to the second question must be: no, different forms of retail ownership do not affect rebate levels. This implies that the chain retailer is presently not able to take advantage of the franchised or unaffiliated retailer through the rebate mechanism, as was alleged. The figures indicate that any retailer, regardless of ownership, may have large or small average rebate levels, but that the franchised and independent retailers benefit from the buying power of their wholesalers. These are also conclusions that were presented previously by the consultants.

3. The third type of analysis, relating rebate levels to the size of all firms regardless of classification, is presented below. The statistics below provide a linear regression model which relates rebate level and company size as measured by retail sales. All twenty-six retail firms surveyed were included in this regression analysis, and over-all rebate levels for each firm are calculated using weights appropriate to product mix. The results indicate clearly that there is no relation between company size and rebate levels, a conclusion that was reached by the consultants previously.

The following are the regression statistics:

$Y = -.085 - .002X$

Where: Y is average rebate level

X is logarithm of sales (in thousands of dollars)

$R^2 = .023$

Adjusted $R^2 = .031$

Standard error of X coefficient = .003

From these analyses, it must be concluded that there is no relationship between levels of rebate and types of retailers. There is also no relationship between rebate levels and sales levels. Therefore, it does not appear that large retailers are using their superior size to obtain buying advantages over smaller competitors in the form of higher rebate levels.

FACTORS AFFECTING REBATE LEVELS

I have set forth the factors affecting rebate levels in point form in order to convey the concepts as clearly as possible.

1. The most important factor affecting rebate levels is that small retailers, particularly the sponsored or franchised retailers, benefit from the buying strength of their wholesaler. Small retailers buy most products from wholesalers whose rebate level is comparable to that of the major chains. Rebates received by wholesalers are entirely passed through to the retailers, either directly or indirectly, as explained in Chapter 8 on wholesalers.

2. The small retailers have more flexible buying policies than the large corporate chains. Such policies allow the small chains to rapidly shift their buying patterns where this may be useful. For example, the small retailer may take better advantage of favourable temporary trade allowances offered by suppliers.

3. A small number of retailers, usually chain retailers, prefer to buy on a bottom-line bargaining basis and consequently have lower over-all rebate levels than otherwise.

4. A very small proportion of large chain retailers' purchases are from wholly-owned manufacturers who sell their entire production to the retailer on a bottom-line basis, resulting in lower total rebate levels than otherwise.

COMPETITIVE ADVANTAGES OF SMALL RETAILERS

Evidence before this Inquiry indicates that the small retailer is not overmatched in competition against the large retailer.

One factor that differentiates the small retailer from the large retailer is the local nature of the small retailer's business. It is possible for the local operator to be more closely in touch with product preferences of his local customers.

A second factor that differentiates the two sizes of retailers is that the owner of a single store frequently operates the store himself, bringing him into personal contact with the community and his customers. This contact may include services -- grocery carrying, check cashing, credit, home delivery and phone-in orders -- which the large retailers do not usually perform. The Retail Merchants Association summarized this difference in their

brief by saying that: "[The small retailers] carry on the old medical tradition of the personal touch, or bedside manner in dealing with a friend who is also their customer."

A smaller retailer may have more pricing flexibility than the large retailer because the former does not follow a weekly head office pricing policy. A small retailer's labour costs are usually lower because his staff is typically not unionized. The small retailer may also use suppliers' labour to stock shelves whereas this is usually forbidden in the labour contracts between the large retailers and their staff. The small retailer has certain tax advantages over the larger retailer and also, if he satisfies certain requirements concerning maximum employment levels, may open on Sundays while the large retailer cannot. These advantages are discussed further in Chapter 13, Concentration and Rebates.

Several small chains have pioneered a number of merchandising techniques, the foremost example of these being the Knob Hill Food Terminal warehousing concept which has now been adopted by some of the large chains. Knob Hill builds large stores each capable of warehousing its own goods, thereby eliminating extra warehouse and delivery expenses.

COMPETITIVE DISADVANTAGES OF THE SMALL RETAILER

1. A small retailer may be at a disadvantage due to his inability to sell wine. While the question of wine

sales may seem to have little connection with rebates, I have heard much evidence on the subject and I am of the opinion that I should consider the problem because of its importance to the small retailer's competitive position.

At present, the Province of Ontario has authorized the sale of Ontario wine in kiosks for supermarkets with store areas in excess of 16,000 square feet.* While I have been using the term "small retailer" according to the number of stores owned, it happens that the large majority of these small retailers are small when considered in terms of store area as well. The Canadian Federation of Retail Grocers estimated in its brief submitted to the Commission that 98% of its membership (most of whom are non-chain retailers) have stores that are less than 16,000 square feet in area.

The Ontario Government's regulation of wine is almost directly contrary to the Quebec Government's regulation of the same product. The Quebec Government has permitted the sale of wine in small retail outlets since 1978. The Quebec law specifies that all holders of a grocery permit are allowed to sell wine in their stores, regardless of store size. The Canadian Federation of Retail Grocers pointed out that small retailers in Quebec who sell wine are able to sell profitably without abuse of liquor legislation. Province-wide wine sales are reported to have risen also which is beneficial to all wines bottled in Canada.

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* Liquor Control Board of Ontario, Revised Directive dated November 1, 1978.

It is a recommendation of this Commission that a revision of the present Ontario regulation be considered with a view to allowing any food retailer to sell wines.

2. A second major disadvantage faced by small retailers is that, frequently, they are not aware of the existence of rebates or are not taking full advantage of the rebates which are offered.

The Commission heard evidence from Mrs. Mae Richardson who is the owner and operator of a retail convenience store in Burlington. Her evidence was that her rebate on milk equalled 5% of her total purchases. Milk prices in Mrs. Richardson's area became a public issue and her 5% rebate level was publicized in the local newspaper. The publicity brought other dairies to Mrs. Richardson's store, each with offers of increased discounts. The original dairy then said they would meet the other offers and subsequently raised Mrs. Richardson's discount from 5% to 14%. The witness testified that she has never been informed whether the discount would increase if she were to increase her volume of milk purchases. Mrs. Richardson also stated that she was unaware whether her bakery supplier offers discounts, allowances or rebates.

Added to this evidence is the evidence of the Commission's consultants.

The consultants conducted a survey of 20 small independent convenience grocery stores, which may also be called "ma-pa stores." The major finding is that the

majority of retailers receive rebates at the maximum level to which they are entitled. However, there is a small proportion (approximately 15% of the sample) of retailers who have an imperfect understanding of the rebate system. The reasons provided for the poor understanding are usually three-fold: the retailer, particularly in urban areas, may have difficulty understanding English; the retailer may have difficulty understanding the idea of a percentage calculation; and the food supplier, particularly the dairy, may give retailers incomplete information.

The Retail Merchants Association of Canada (Ontario) Incorporated observed in its brief that a number of small retailers are not fully aware of all the rebates or terms of rebates available to them.

3. Several witnesses before this Commission testified that one of the most serious disadvantages plaguing the small retailer is disadvantageous site location. Not only do financial resource limitations prevent the small retailer from securing desirable site locations, but there may be restrictions in leases between developers and food retailers which prevent other food retailers from locating within a distance specified by the lease. This topic and topics such as advertising economies and other economies of scale are treated more fully in Chapter 13 on concentration.

In summary, it seems that a legitimate case could be put forward that present legislation relating to the sale of wine in Ontario discriminates against owners of stores

that are smaller than 16,000 square feet. It also seems that some smaller retailers may not fully understand the rebate system. Finally, it seems that some suppliers do not adequately inform their customers of the rebates offered.

CONCLUSIONS

The following summarizes my conclusions on the evidence examined in this chapter:

1. There is no exact definition of a small retailer. There are, in fact, seven types of stores which can be considered small retailers.

2. In Ontario, 7,702 stores are classified as small retailers and 689 as large retailers.

3. Most Ontario retail food sales are made by the large retailers.

4. Between 1969 and 1979, the market shares of group independents and unaffiliated independents declined sharply during the first six years of this period and more slowly during the last five.

5. There is no statistically significant difference in the gross margin, net margin after tax or return on equity between the large and small retailers sampled.

6. There is no significant difference in rebate levels between large and small retailers, when averages weighted according to product mix are considered.

7. The large retailer is presently not able to take advantage of the smaller retailer through the rebate mechanism, despite allegations to the contrary.

8. The data in evidence indicates that any retailer, regardless of size, may have high or low average rebate levels, but that small retailers benefit from the buying power of their wholesalers. Thus, goods purchased by the small retailer, on average, carry the same rebate as similar goods purchased by the large retailer.

9. Smaller retailers have the following competitive advantages over the chains:

   (a) better knowledge of the product preferences of their customers;
   (b) more personalized service;
   (c) greater selling and buying flexibility;
   (d) lower wage scales;
   (e) greater ability to require suppliers to provide certain labour-related services;
   (f) more tax advantages;
   (g) absence of restrictions in regard to store hours.

10. The chains have the following competitive advantages over smaller retailers:

(a) greater media advertising;

(b) better understanding of the rebate system;

(c) greater access to capital;

(d) better store locations;

(e) ability to offer wine to consumers.

11. Despite the disadvantages listed in the paragraph above and considering all aspects of the small retailer's operation, it does not appear that the small retailer is unable to compete with larger competitors. This conclusion is reinforced by the evidence of small retailers themselves in respect of their ability to compete. I will consider the qualification expressed by one retailer in Chapter 14, Loss-Leader Selling.

RECOMMENDATION

1. The ability of large retailers to sell wine appears to be an advantage enjoyed by the large retailers. It is recommended that the Legislature consider the feasibility of permitting small retailers to sell wine.

CHAPTER 11

NAME BRANDS, HOUSE BRANDS AND REBATES

NAME BRANDS, HOUSE BRANDS AND REBATES

GENERAL

In Chapter 5 dealing with processor/manufacturers and rebates, a survey of ten leading brands of 87 food processors was presented. This survey disclosed that processors obtain 86% of sales from name brand and the remaining 14% from house brand products. In this chapter, I shall consider the differences in prices and rebates between these two classifications.

"Name brands" are products sold to consumers bearing the manufacturer's name or trade name on the label. "House brands" are products sold to consumers bearing the retailer's name or trade name on the label. The term "house brands", as used in this chapter and throughout this report, includes the "generic" or "no-name" products bearing labels which identify neither the retailer's nor the processor's name or trade name but simply the contents of the package. For the purposes of this chapter, I have considered generic products to be merely a subclass of house brand products because both generics and house brands are treated similarly from the standpoint of prices and rebates.

Generally, only the large chains carry house brand products; the smaller retailers deal almost exclusively in name brand products.

PRICE AND REBATE DIFFERENTIAL BETWEEN NAME AND HOUSE BRANDS

The processors surveyed reported that house brands are sold to retailers at a price that is, on the average, 14.4% lower than the price of comparable name brand products. This percentage is calculated on a net-price basis which includes all discounts, rebates and allowances.

The retailers surveyed reported that house brands are sold to consumers in the Metropolitan Toronto area at a price that is 15.5% lower than the price of comparable name brand products. One urban market, Metropolitan Toronto, was selected in order to obtain survey results from market conditions which are as uniform as possible.

The average rebate level reported on name brand products is 10.6% of sales from suppliers to retailers, and on house brands, 4.3% of sales. This reflects a difference between the two classifications' rebate levels of 6.3%.

Table 11-A reflects these findings.

RATIONALE FOR PRICE AND REBATE DIFFERENTIALS

Processors interviewed provided several reasons for the lower selling price of house brand products. These reasons are presented in point form as follows:

1. New name brand products require considerable expenditures for research, development, production facilities and market creation. House brand products rarely

TABLE 11-A

NAME AND HOUSE BRAND PRICE AND REBATE DIFFERENCES

	Name Brand Product	House Brand Product	Difference
Manufacturer's Net Selling Price (Including all rebates) (100 base)	100	85.6	14.4%
Rebate level (% of Manufacturer's sales)	10.6%	4.3%	6.3%
Retailer's Selling Price to Consumers (100 base)	100	84.2	15.8%

NOTE: All off-invoice allowances are included in these figures.

SOURCE: Retailer and processor/manufacturer questionnaires.

incur any of these expenses or the risks associated with new name brand product introduction.

2. A name brand product requires a continuing expenditure of advertising dollars to maintain consumer awareness of the name brand. House brands require little, if any, advertising or selling expenditures.

3. House brand products are often the result of excess capacity use; consequently, manufacturers may price them so as to recoup only the variable or marginal costs, not the fixed costs or costs of development.

4. House brand products represent a lower risk to the manufacturer because the selling risk is assumed by the retailer. House brands are "guaranteed" sales for manufacturers because they are usually produced under contract. This lower risk may be reflected in the lower margin component of the manufacturer's price to the retailer. The manufacturer is able to plan production very accurately with knowledge of the exact volume to be produced.

5. Production and distribution are cheaper for house brand products because these functions are usually performed on a bulk basis.

6. The house brand products are frequently made of lower quality ingredients or with cheaper processes than name brand products.

It should be remembered that these are not the Commission's conclusions. They are simply the reasons provided by the processors interviewed, just as the points which follow are reasons provided by the retailers and are not the findings of the Commission.

The retailers' reasons for price differences to consumers between name and house brands are as follows:

1. House brand products, purchased from suppliers on a contract basis, cost retailers less to buy than equivalent name brand products. This is true both before and after rebates are calculated.

2. House brand products are usually products for which there is already a high degree of consumer acceptance. Thus, house brands benefit from larger advertising expenditures incurred by name brands.

3. A related point is that new house brand products are more likely than new name brand products to benefit from the advertising of existing products. This is because new name brands must establish more characteristics, such as reputation and quality, than new house brands must establish.

4. Consumers buying house brand products consider price to be the major determinant in their choice of product whereas consumers buying name brand products may consider other characteristics, such as reputation and quality, emphasized by name brand advertising.

Consequently, competition between house brand products will be mainly on the basis of price.

5. The house brand segment of the retail market is more price sensitive than the name brand segment, and consequently, the price of similar competing products will have a large influence on the pricing decision.

6. Because consumers may more closely identify house brand products with the retailer rather than with the processor, retailers price house brands lower in order to maintain the low-price image they are hopeful of promoting.

7. Handling and warehousing costs are generally lower for house brand products than for name brand products because house brands are generally purchased in greater quantities than name brands.

These factors vary considerably in importance with respect to the final pricing decision made by each firm about every product in each market area. The lower cost to retailers of house brands is only one factor among many market factors that determine the final price.

CONCLUSIONS

1. House brand products are sold by manufacturers to retailers for less than comparable name brand products. In turn, retailers charge consumers

less for house brand products than for name brand products.

2. The average rebate level for name brand products is 10.6% of sales whereas the average rebate level for house brand products is 4.3% of sales.

3. Lower costs of production, advertising and selling result in both lower rebate levels granted by, and lower net selling prices paid to, manufacturers for house brand products relative to name brand products. Market factors, as well as lower costs, enable retailers to offer house brand products more cheaply to consumers than name brand products.

CHAPTER 12

COST JUSTIFICATION OF REBATES

GENERAL

In the Resources Development Committee hearings held prior to this Inquiry, it was alleged that rebates are entirely unrelated to costs. It was alleged, instead, that rebates are obtained by coercion. In Chapter 5, Processor/Manufacturers and Rebates, I have dealt with the "coercive" aspect of this allegation. The "cost justification" aspect remains to be dealt with.

Although the concept that rebates should be cost justified is not strictly within the terms of reference, I felt it should be considered. Several witnesses expressed the opinion that rebates offered by a supplier to a buyer should be equal to the cost benefit to the supplier. Cost justification of rebates has been the subject of considerable comment in previous food industry studies. The United States Clayton Act, as amended by the Robinson-Patman Act, by legislation, imposes a cost-justification standard upon negotiations between suppliers and retailers in that country. This provision will be considered in Chapter 16 of this report.

I will give an example of the cost-justification concept as it currently operates in the United States in order to explain it. A warehouse allowance is paid by a supplier to a buyer on the condition that the buyer performs a warehousing service. The costs of this service include

long-term costs of building and financing the warehouse as well as short-term operating costs. Cost justification would allow the buyer to charge the supplier an amount equal to certain judicially defined costs of the warehousing service, but no more, as the warehouse allowance.

It must be remembered, when considering the concept of cost justification in rebates, that there is no federal or provincial law that presently requires a supplier or buyer in Ontario to cost justify a rebate.

EVIDENCE AND SUBMISSIONS RELATING TO COST JUSTIFICATION

The evidence and submissions of the various organizations to the Inquiry were quite contradictory on this issue. I will deal with each of the allegations individually.

The view of the Ontario Federation of Agriculture, as presented in its submissions, is that the entire system of discounts and allowances is a reflection of the buying advantages which large retail organizations have in Ontario. The Federation further submitted that what has been notably absent is any real economic explanation for the level of discounts.

The leader of the Ontario Liberal Party, Dr. Stuart Smith, submitted that the lack of a cost-justification standard for the legitimacy of rebates is a major failing of the Combines Investigation Act, rendering the federal

legislation "virtually unworkable" in the prevention of discriminatory pricing practices.

This allegation will be treated in Chapter 16 on rebates and the law. However, it is not out of place to mention at this point the testimony of Mr. Robert Bertrand, Director of Investigation and Research under the Combines Investigation Act. This witness pointed out that not only would cost-justification legislation impose a cost on business obligating firms to pay for cost-justification studies in their own defence, but also such legislation would impose an inflationary factor on society if firms become reluctant to reduce prices for fear that they may later have to cost justify such reductions.

Industry itself may be said to be divided as to the effects of cost-justification standards. Two witnesses testifying in favour of cost justification -- the retailer, Mr. Carl Quaranto, and the wholesaler, Mr. Geoffrey Holt -- have had experience, albeit brief, in the United States food industry. It is their impression that cost justification has resulted in business practices in that country which are less discriminatory than exist here.

Such testimony is balanced by the considered submissions of the Grocery Products Manufacturers of Canada, the Retail Council and two major chains opposing the introduction of cost-justification legislation.

The Retail Council points out that the "cost" of cost justification would fall substantially on manufacturers

faced with the task of assigning and recording costs for each specific operational function. This task would be particularly onerous for smaller companies. The conclusion reached is that the cost-justification approach will lead to reduced competition, a conclusion with which the G.P.M.C. concurs.

The brief of Dominion Stores Limited outlined some of the savings which, the firm submits, are reflected in rebate payments. I have paraphrased relevant sections of their submission, as follows.

Volume discounts properly reflect economies of scale in the production and delivery of goods. The greater the volume purchased by the chain, the lower is the unit cost of the supplier. This cost reduction should be reflected in savings to the retailer and, ultimately, to the consumer.

Promotional allowances recognize the food retailer's ability to effectively promote products to the consumer. The retailer's promotional activity greatly increases the sales volume of the products to the benefit of both the retailer and the supplier. It allows particularly the small supplier to benefit from the large-scale advertising which the food retailers undertake, the costs of which would otherwise be far beyond this supplier's economic capability.

Other marketing efficiencies derive from the large warehousing facilities operated by major food retailers and wholesalers. Such facilities allow suppliers to take advantage of the cost efficiencies in truck-load and car-load deliveries as opposed to smaller unit sales.

The testimony of Mr. David Nichol, President of Loblaws Limited, supported the contention that suppliers receive full value for rebate payments, a contention that manufacturers almost universally concurred with, I might add. He stated that cost justification as practiced in the United States would increase costs in any distribution system.

Professor Lawrence A. Skeoch and Mr. Bruce C. MacDonald were commissioned by the Federal Government to conduct a comprehensive study of Canadian Combines Legislation published in 1976. Their report entitled Dynamic Change and Accountability in a Canadian Market Economy dealt, amongst other things, with the subject of cost justification in rebates. In considering the issue of whether cost-justification legislation should be enacted, they concluded that such legislation would favour large buyers. I quote from this report:

> "If the large buyers were entitled by law to justified differentials, they would demand the full amount of the economic advantages - both on the cost side and the elasticity of demand side - that could be associated with their purchases. There is persuasive evidence that if they did so,

price differentials would increase rather than diminish...In our view, a case cannot be made for special price discrimination legislation to protect small business, both because the general grounds advanced for such protection are not persuasive and also because the longer-run side effects of the attempt to provide it are detrimental to the ecomony."*

The longer-run side effects referred to are the possibilities that a large buyer may: 1) set up his own facilities to process, 2) take over existing firms, or 3) absorb their entire output.

Simply stated, to recommend legislation requiring cost justification of rebates would not benefit the farmer and could adversely effect the consumer. Such legislation would, in my view, stifle competition and result in higher consumer prices.

Further research on this issue is provided in the work of the Inquiry's consultants.

I summarize their findings in point-form as follows:

1. Answers to the processors' questionnaire and interviews with processors indicate that,

* Lawrence A. Skeoch with Bruce C. McDonald, Dynamic Change and Accountability in a Canadian Market Economy, (Ottawa: Minister of Supply and Services Canada, 1976), pp. 212-216.

especially for medium- and small-sized firms, there is no accounting system in place which could provide details of the dollar value of cost savings. This is because many of the costs are intangible or difficult to allocate.

2. Similarly, in respect of small and large retailers, there are no systems currently in place that accurately record exact costs of retailers' services. This is also because many of the costs are intangible or difficult to allocate.

3. Because precise calculation of cost savings associated with rebates is so difficult, there would be a considerable expense incurred by the food industry if cost justification were to be required. It is certain that this expense would eventually be passed through to the consumer.

CONCLUSIONS

The following summarizes my conclusions on the evidence examined in this chapter:

1. There are widely divergent views as to the need for legislation requiring the cost justification of rebates. I share the view of the Grocery Products Manufacturers that such a legislative requirement would inhibit the natural operation of a free market and would lead to reduced competition.

2. In general, all rebates have an element of cost justification in their origins, but considerably more market factors than cost savings enter into the final determination of a rebate level.

3. It is not feasible for this Commission to determine whether or not rebates are fully cost justified. Processors, wholesalers and retailers do not have accounting systems in place to provide the necessary information. For the Commission itself to attempt to acquire the necessary data would involve excessive time and expense.

4. The effect on the farmer of legislation requiring cost justification may be that competition among processors and retailers would be reduced. In this case, farm prices may be adversely effected.

5. Legislation requiring cost justification would burden processors with the task and expense of justifying price reductions. In this case, the expense would likely be passed through to the consumer and processors would become reluctant to reduce prices. If these assumptions are correct, consumer prices would be adversely affected.

CHAPTER 13

CONCENTRATION AND REBATES

GENERAL

A large amount of evidence given before this Commission focused on the issue of concentration in the Ontario food industry. It will be noted that the word "concentration" does not appear in the Commission's terms of reference. Nevertheless, the Commission accepted most, if not all, of the evidence tendered on this subject for the reasons discussed below.

The Members of Parliament on the Standing Resources Development Committee, whose recommendations led to the formation of this Inquiry, were very concerned about concentration and its effects on the food industry. They reported their concern that "...[t]he concentration of power in the hands of the five chains spells the death knell of the independent grocer to whom the chain discounts are not available....The power in the hands of the chain will in turn reduce the competition among processors if the smallest processors are unable to absorb the discounts."*

Concern about concentration was repeatedly expressed throughout the Commission hearings. This issue preoccupied the submissions of organizations as diverse as the Ontario Federation of Agriculture, the Consumers Association of Canada, and the Canadian Federation of Retail Grocers.

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* Report of the Standing Resources Development Committee, June 23, 1978, page 3.

Many economic theorists, but not all, share the concerns expressed in these submissions. Their theories predict that excess levels of concentration have adverse effects on the economy. Of particular consequence concerning our terms of reference are their predictions that consumers must pay higher prices for commodities sold by industrial sectors which are excessively concentrated. They also predict that excessive concentration among buyers will force prices of commodities sold to the concentrated sector to decline to the detriment of the producer.

The Commission is charged with the duty of determining what effect discounting has on prices paid by consumers and on prices paid to producers. Therefore, if discounting does increase concentration and if concentration in turn does have an adverse effect on consumers and the economy, the issue of concentration is well within the Commission's reference and may indeed be one of the critical issues the Inquiry must face.

However, I hasten to add that this chapter is not a study in depth of concentration in the food industry at its various levels. A subject of this significance could well be the subject of a separate inquiry.

1. ECONOMIC THEORY OF CONCENTRATION

The purpose of this section is to set out accepted economic criteria which will permit me to evaluate allegations that the food industry is, or is becoming, excessively concentrated.

The determination as to whether consumers are paying more than they should for food products, and whether farmers are being paid less for food products than they should be paid, is expressed by the economist to be a determination of "market performance." In order to better understand "market performance," economists turn to "market structure" and to "market conduct."

The economist assists the policy-maker by ascertaining the relationship of each of these three notions to the other two, in the same way that a medical doctor analyzes the human body. Just as the physician takes the patient's temperature or blood pressure to monitor performance, so the economist is concerned with market performance. If performance is abnormal, the doctor will investigate the conduct or functioning of the digestive and respiratory system; the economist likewise will investigate the conduct of the industry. Alternatively, the doctor will check to see if the structure is sound -- whether any bones or organs are broken or otherwise harmed; similarly, the economist will investigate structural imperfection.

A. MARKET STRUCTURE

The most important structural feature in analyzing markets is the degree of concentration of sellers and buyers. A market is categorized loosely by the number of sellers and buyers as follows:

Number of Sellers	Type of Market	Number of Buyers	Type of Market
One	monopoly	One	monopsony
Few	oligopoly	Few	oligopsony
Many	atomistic competition	Many	atomistic competition

A monopolist/monoposonist has considerable latitude in choosing prices and output. At the other extreme, an atomistic seller has no influence over prices or output. In the middle of this range, oligopolists/oligopsonists have the potential to control industry output or prices: they may exert the same control over price and output exerted by monopolists if there is perfect collusion among them. However, oligopolies/oligopsonies may result in prices and outputs virtually identical to that of atomistic competition if there is no collusion between sellers. There may also be any range of prices and output between those pertaining in monopoly and in atomistic competition which would indicate imperfect collusion.

The customary measure of concentration is firm market share. This figure expresses the percentage of the total market held by a group of firms. The number of firms in this group most frequently chosen by economists is four. The higher the four-firm market share, the more concentrated is the market. Following is a categorization

developed by a widely respected economist* which will be used throughout this chapter to compare degrees of competition:

Description	Top 4-firm Market Share
very high	76 - 100%
high	65 - 75%
moderately high	50 - 65%
moderately low	35 - 50%
low	25 - 35%
very low	0 - 25%

Other structural aspects of a market may also assist in explaining why the market is as concentrated as it is.

"Barriers to entry" refers to obstacles that a potential new firm must overcome before beginning to operate in the industry. For example, potential new entrants to food retailing may not be able to secure a viable site location for a variety of reasons.

"Product differentiation" describes the extent to which one product is different from another product, for example, in design or performance. In fact, differentiation occurs if marketers of a product successfully convince consumers that the product is unique even though it may not be substantially different. The more unique a product is, or appears to be, the more control its marketers will have over price and output.

* Joe S. Bain, Industrial Organization (New York: Wiley, 1968), page 140 ff.

Geographic structures affect concentration by eliminating potentially competitive products which cannot feasibly be transported into the market in question. Product durability similarly affects concentration in the food industry. Examples of the effects of geographic structures and product durability are the milk and bread industries: consumer demands for fresh milk and bread encourage daily deliveries to the store door and discourage transportation from distant points.

"Market growth" refers to increasing demand for a product which may well make the industry attractive to firms not currently producing a product, thus decreasing concentration. Legal structures may prevent mergers of competitors, thus diminishing the likelihood of increasing concentration.

"Vertical integration", yet another aspect of market structure, refers to one firm's ownership of, or legal interest in, a second firm from which the first firm obtains supplies necessary to conduct its business. This situation may be reversed where the supplier owns or has an interest in the supplied firm. The term "vertical integration" is distinguished from the term "horizontal integration" which refers to ownership of or interest in a competitor at the same level in the marketing chain.

B. <u>MARKET PERFORMANCE</u>

An economist measures market performance by comparing selling prices to costs of production, a comparison stated

by the profit rates of the firms in the industry. A market that is performing well is called "efficient"; that is, such a market will produce more and better products at lower prices than markets that are "inefficient," and firms in the efficient market will earn normal profits for the degree of risk that similar firms face.

The economist uses criteria other than profit rates to measure efficiency as well, such as: utilization of existing capacity, the ratio of sales promotion costs to sales revenue, progressiveness of production techniques, conservation of resources, and price flexibility. Unfortunately, quantitative data providing such information is not usually available to the economist. Even where such data is available, the economist is not likely to have acceptable standards against which the data can be evaluated. Profit rates, on the other hand, are made available to the economist through government and corporate reporting of accounting measures of profit.

C. MARKET CONDUCT

Discounting is but one aspect of "market conduct." Market conduct is mainly concerned with determination of price and output. In studying conduct, the economist is seeking to discover patterns of behaviour -- how a firm interacts with other firms at its level and at other levels in the industry. Is the firm able to influence the price and output of its competitors? Is it able to coerce better terms from its suppliers? I examine discount-related

aspects of food retailers' conduct in other chapters, such as the listing and delisting of products (Chapter 15).

I have now examined briefly the notions of market structure, market performance and market conduct. The knowledge that an industry's market structure is oligopolistic rather than atomistic, that its profit rates are high rather than low, alerts the economist to watch out for certain behaviour patterns. However, market-behaviour patterns must actually be observed, and their effect on the industry's structure and performance verified, before the economist pronounces as to the industry's well-being.

2. CONCENTRATION AT THE PRODUCER LEVEL

The farm sector operates under structures which range from atomistic or pure competition in some products to absolute sellers' monopoly in other products subject to marketing boards.

A marketing board that controls the conduct of its producer members exhibits structural characteristics of a monopoly in that all producers act as if they were one producer. A board may control the conduct of its producers through price setting, through allotment of supply quotas or through co-ordination of advertising and promotion. Co-ordination of advertising and promotion is not as powerful an element of market control as is price setting and supply management. Table 13-A in this Chapter sets out a list of marketing boards ranked in order of increasingly monopolistic powers. However, marketing boards are a unique type of

TABLE 13-A

ONTARIO MARKETING BOARDS' POWERS

Powers Available		Board
Product promotion	1.	Fresh Potato Growers' Marketing Board
Price Negotiation and Product Promotion	1.	Berry Growers' Marketing Board (presently does not use price negotiation powers)
	2.	Grape Growers' Marketing Board (Processing)
	3.	Potato Growers' Marketing Board (Processing) (no promotional function)
	4.	Processing Tomato Seedling Plant Growers' Marketing Board (no promotional function)
	5.	Seed Corn Growers' Marketing Board (no promotional function)
	6.	Soya Bean Growers' Marketing Board
	7.	Vegetable Growers' Marketing Board (Processing)
Price Establishment and Product Promotion	1.	Apple Marketing Commission
	2.	Asparagus Growers' Marketing Board
	3.	Bean Producers' Marketing Board
	4.	Fresh Grape Growers' Marketing Board
	5.	Greenhouse Vegetable Producers' Marketing Board
	6.	Pork Producers' Marketing Board
	7.	Rutabaga Producers' Marketing Board
	8.	Tender Fruit Producers' Marketing Board
	9.	Wheat Producers' Marketing Board (no promotional function)
Production Quotas and Price Establishment	1.	Burley Tobacco Growers' Marketing Board (minimum price only)
	2.	Chicken Producers' Marketing Board
	3.	Cream Producers' Marketing Board (price negotiation)
	4.	Egg Producers' Marketing Board

TABLE 13-A (continued)

Powers Available	Board
Production Quotas and Price Establishment (continued)	5. Flue-cured Tobacco Growers Marketing Board (minimum price only) 6. Milk Marketing Board 7. Turkey Producers' Marketing Board

SOURCE: Ontario Ministry of Agriculture and Food

monopoly, formed by the Legislature for the purpose of achieving balance between many small (atomistic) sellers and few (oligopolistic) buyers, and for the purpose of achieving stabilization of farm incomes at adequate levels. Table 3-A in Chapter 3 sets out the values of the various crops regulated and not regulated by marketing boards.

On the buying side of the farm market, farm products in the livestock and field crop categories are generally sold to processors or wholesalers, the majority of whom are very large compared to the individual producer. In the fresh fruit category not covered by marketing boards, 19%, or $2,434,000, of the 1977 crop was sold to chain stores. In the vegetable category not under marketing board control, 60%, or $50,456,000, was sold to chain stores.* In these categories especially, producers -- the fruit and vegetable growers -- are selling to buyers with generally superior bargaining power. Furthermore, these buyers, as we shall see in later sections, are generally situated in relatively concentrated industries.

This finding is balanced by the fact that Ontario farms are becoming increasingly concentrated in terms of numbers, size and value of output. In Ontario, the number of farms declined from 90,438 in 1961 to 76,983 in 1976. During the same period, the proportion of farms over 399 acres in size increased from 5.5% of all farms to 9.7% of all farms. The largest 15% of Ontario farms (ranked by value of agricultural produce sold annually) produced 60%

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* Ontario Ministry of Agriculture and Food. Also Figure 3-B, Chapter 3 in this Report.

of all Ontario agricultural produce in 1961, a figure that increased to 65% in 1976.*

In addition, this Commission heard evidence of relatively high barriers to entry into agriculture. Estimates of capital requirements for a thirty-acre fruit farm ranged from $300,000 to $400,000 and for a similar size vegetable farm, $200,000 to $300,000.† In products which have supply-management quotas, the cost of quotas is a further barrier to entry.

On the basis of the above data, it appears that the historical picture of an atomistic market structure in agriculture may be less and less a realistic one. In fact, it appears that the producer level of the food chain is becoming increasingly concentrated.

My evaluation of market structure and conduct at the producer level now proceeds to an examination of the performance measures of farm prices and farm incomes.

In the most recent study of farm incomes reviewed by the Commission, the principal finding is that farm returns for the 1971-1974 period, including capital gains, are "quite similar" to non-farm returns.** The significance

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* Statistics Canada, catalogue #96-806, and estimates provided by the Economic Branch, Ontario Ministry of Agriculture and Food.

† Howard Staff, President, Ontario Fruit and Vegetable Growers Association, Transcript: vol. 2, pp. 58-59.

** J.A. Gellner and G.L. Brinkman, Relative Rates of Resource Returns on Ontario Commercial Farms, 1971-74 (University of Guelph: September, 1977).

of this finding is that it is wrong to assume that Canadian farmers are generally unable to earn an adequate income from farming operations. It is suggested in this study that farms producing products controlled by marketing boards have higher returns than other farms. All types of farms show very large yearly income variations.

While this Commission did not investigate agricultural prices in depth, reports in this area were reviewed. The price performance of the agricultural sector in Canada has often been criticized. For example, the final report of the Food Prices Review Board noted that commodities subject to supply-management boards tended to exhibit higher prices and costs.*

In summary, this Commission finds that concentration at the producer level ranges from atomistic to monopolistic, and is increasing, though I cannot say in which commodities. I further recognize that the ability to form a marketing board is available to all Ontario producers pursuant to the provisions of <u>The Farm Products Marketing Act</u> and <u>The Milk Act</u>.†

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* Food Prices Review Board. <u>Telling It Like It Is</u> (Ottawa: February, 1976).

† <u>Farm Products Marketing Act</u>, R.S.O. 1970, c. 162, s.5; and <u>The Milk Act</u>, R.S.O. 1970, c. 273, s.6. Both statutes provide that a representative group of producers may petition the respective boards to establish a plan for the control and regulation of the marketing of farm products.

3. CONCENTRATION AT THE PROCESSOR LEVEL

The Ontario Federation of Agrculture alleged that rebates increase concentration at the processor level. Their view of the effect that discounting has on the structure and performance of the processor and subsequent levels is paraphrased as follows: pressured for rebates benefitting the large buyers, the processor is unable to reduce its prices generally, in which case it loses buyers and eventually falls out of the market. Alternatively, the processor is obliged to restructure its price list upwards in order to achieve sufficient returns, in which case smaller customers paying list price without discounts or with minimal discounts are seriously disadvantaged. The result, in either case, would be increased concentration.

Concentration would also be increased by the practice of giving volume rebates, theorized the O.F.A., because chain stores are encouraged to buy a given product from only one processor in order to achieve the processor's maximum rebate level. High concentration has an adverse effect on the farming sector which depends on effective markets for its vitality. High concentration also has an adverse effect on the consumer who depends on a competitive processing sector for choice of, and innovation in, product supply. The validity of the O.F.A.'s concerns depends on the answers to two questions:

(1) How concentrated is the processing sector?

(2) What role does discounting play, if any, in respect of concentration?

An examination of the structure of the food processing industry reveals high levels of concentration in certain product lines. Table 13-B shows four-firm and eight-firm market shares for several processing industries as well as names of leading firms in these industries with substantial operations in Ontario. As noted in the Table, these firms are not ranked in the order of their market share. Using the classification set forth in the first section of this chapter, we see from the Table that sugar processing is very highly concentrated. Biscuit, frozen fruit and vegetable, flour and breakfast cereal manufacturing are all highly concentrated. Bakeries and dairies are moderately concentrated. A recent industry study points out that food manufacturing levels of concentration are similar to those of all manufacturing sectors in Canada.*

Caution must be exercised when using these figures because they are expressed on a national basis while the relevant market for perishable products is often provincially based or smaller. Bakery products, for example, are very perishable and cannot be transported successfully over long distances; consequently, the relevant market is a regional market rather than a national market. Unfortunately, reliable provincial and regional figures are not available.

The barriers to entry are generally lower in food manufacturing than they are in other manufacturing

* R.M.A. Loyns, Farm to Food Prices, Discussion Paper 157, prepared for the Centre for the Study of Inflation and Productivity (January, 1980).

TABLE 13-B

LEADING FIRMS AND MARKET SHARES IN PROCESSING INDUSTRIES

Year	National Market Share Top 4 Firms	Top 8 Firms	Major Firms with Ontario Operations*
1011 Slaughtering and Meat Processors			
1976	49.5	59.9	Canada Packers Limited ("York Farms", "Maple Leaf", "Swift Premium", "Lazy Maple", "Sugar Plum")
1970	54.8	63.3	Swift Canadian Company
1965	61.8	67.5	J.M. Schneider Incorporated
1012 Poultry Processors			
1976	38.0	53.7	United Co-operatives Limited
1970	37.0	53.3	Swift Canadian Company Limited ("Butterball Swift Premium")
1965	26.9	40.3	Canada Packers Limited
102 Fish Products Industry			
1976	49.0	59.6	National Sea Products Limited ("High Liner")
1970	39.2	52.2	
1965	35.6	50.6	
1031 Fruit & Vegetable Canners & Preservers			
1976	39.3	54.7	Campbell Soup Company
1970	41.7	57.6	H.J. Heinz of Canada Limited
			Canadian Canners Limited ("Aylmer", "Del Monte")
			Pillsbury Canada Limited ("Green Giant", "Clarke", "Niblets")

TABLE 13-B

LEADING FIRMS AND MARKET SHARES IN PROCESSING INDUSTRIES (continued)

Year	National Market Share Top 4 Firms	Top 8 Firms	Major Firms with Ontario Operations*
			Libby McNeil & Libby of Canada Limited ("Bird's Eye") Canvin Products Limited ("Allen's", "Mitchell's", "Canada White") Robin Hood Multifoods Limited ("Bick's") E.D. Smith & Sons Limited
1032 Frozen Fruit & Vegetable Processors			
1976	x	76.4	Pillsbury Canada Limited ("Green Giant")
1970	x	x	Libby McNeil & Libby of Canada Limited Minute Maid Corporation of Canada Limited
104 Dairy Products Industry	37.3	49.3	Dominion Dairies Limited ("Sealtest", "Light N' Lively") Beatrice Foods (Canada) Limited Silverwoods Industries Limited Donlands Dairy Limited Becker Milk Company Limited
105 Flour & Breakfast Cereal Products Industry			
1976	66.2	85.1	Maple Leaf Mills Limited ("Purity", "Monarch", "Red River")
1970	70.1	87.7	Weston Companies Robin Hood Multifoods Limited Quaker Oats of Canada Limited ("Aunt Jemima") General Mills Canada Limited ("Cherrios", "Betty Crocker", "Pop Tarts", "Wheaties")

TABLE 13-B

LEADING FIRMS AND MARKET SHARES IN PROCESSING INDUSTRIES (continued)

Year	National Market Share Top 4 Firms	Top 8 Firms	Major Firms with Ontario Operations*
			General Bakeries Limited ("Hostess")
			Kellogg-Salada Company (Canada) Limited
			General Foods ("Post") Limited
			Christie Brown & Company Limited ("Nabisco", "Shredded Wheat")
			Proctor & Gamble Company of Canada Limited ("Duncan Hines")
			Pillsbury Canada Limited
106 Feed Industry			
1976	27.2	37.1	
1970	29.4	39.9	
1965	28.8	38.9	
1071 Biscuits Manufacturers			
1976	73.6	91.6	Weston Companies ("McCormick")
1970	68.1	83.9	Christie Brown Limited
1965	67.2	83.6	Associated Biscuits of Canada Limited ("Peek Frean", "David", "Huntley & Palmers")
1072 Bakeries			
1976	31.9	45.6	Weston Companies
1970	31.6	44.8	General Bakeries ("Home Price", "Wonder Bread", "Hostess")
1965	32.2	43.8	Corporate Foods Limited ("Dempster's" "ToastMaster")

TABLE 13-B

LEADING FIRMS AND MARKET SHARES IN PROCESSING INDUSTRIES (continued)

Year	National Market Share Top 4 Firms	Top 8 Firms	Major Firms with Ontario Operations*
1081 Confectionery Manufacturers			
1976	51.2	74.6	Dare Foods Limited
1970	52.8	72.4	Wm. Neilson Company Limited
1965	46.6	65.4	Catelli Limited ("Laura Secord")
			McNair Products Company Limited
			Rowntree Mackintosh Canada Limited
			Warner-Lambert Canada Limited ("Adams", "Certs", "Chiclets")
			Wm. Wrigley Jr. Company Limited ("Juicy Fruit", "Spearmint", "Standard Brands Limited", "Lowney's", "Moirs")
			Standard Brands Limited ("Lowney's")
1082 Cane & Sugar Beet Processors			
1976	x	100.0	Redpath Sugars
1970	x	-----	Atlantic Sugar ("Lantic")
1965	x	100.0	Sucronel Limited
			Westcane
1083 Vegetable Oil Mills			
1976	87.1	-----	Canada Starch Company ("Mazola", "Crown Brand", "Hellman's", "Karo", "Benson's")
1970	78.5	x	St. Lawrence Starch Company Limited ("Bee Hive", "Durham")
1965	x	x	Standard Brands Limited ("Fleishman's", "Blue Bonnet")

TABLE 13-B

LEADING FIRMS AND MARKET SHARES IN PROCESSING INDUSTRIES (continued)

Year	National Market Share Top 4 Firms	National Market Share Top 8 Firms	Major Firms with Ontario Operations*
			Proctor & Gamble Company Limited ("Crisco")
			Canada Packers Limited
			Monarch Fine Foods Company, Limited ("Imperial")
1089 Miscellaneous Food Processors NES			
1976	37.8	53.1	General Foods Limited ("Minute Rice", "Maxwell House", "Sanka", "Kool Aid", "Tang", "Jell-O")
1970	33.7	50.2	Standard Brands Limited ("Chase & Sanborn", "Royal Desserts")
1965	x	x	Cheesebrough Pond's (Canada) Limited ("Adolph's", "Roger")
			Reckitt & Colman Canada Incorporated ("French's", "Worcestershire")
			Canada Starch Company Limited ("Skippy Peanut Butter", "Chefmate")
			Campbell Soup Company ("Swanson")
			Robin Hood Multifoods ("Stouffer's")
			Catelli Limited ("Catelli/Romi", "Habitant")
1091 Soft Drink Manufacturers			
1976	50.7	61.3	Coca-Cola Limited ("Fanta", "Sprite", "Tab", "Fresca")
1970	46.0	54.5	Pepsi-Cola Canada Limited ("Mountain Dew", "Team", "Patio Flavours", "Niagara Dry")
1965	40.8	48.0	Crush International Limited ("Quirst")

TABLE 13-B

LEADING FIRMS AND MARKET SHARES IN PROCESSING INDUSTRIES (continued)

Year	National Market Share Top 4 Firms	National Market Share Top 8 Firms	Major Firms with Ontario Operations*
			Seven-Up Canada Limited Canada Dry Limited ("Hires", "Pure Spring", "Royal Crown", "Wilsons")

NOTE: *Firms are not ranked in order of market share and may not be in top 4 or top 8 firms for which market share is indicated.

SOURCE: Statistics Canada, Industrial Organization and Concentration in the Manufacturing Industries of Canada, 1976 (Preliminary) except column "Major Firms with Ontario Operations" which Commission staff developed from various trade sources.

industries. Economic barriers to entry -- technological complexity, capital requirement, economies of scale, brand identification and advertising intensity -- are reported to be lower in food manufacturing than in other manufacturing industries.* Regulation barriers -- licensing of dairy plants, review of foreign investments by Foreign Investments Review Agency -- are not severe at present. These factors signify that market share statistics tend to overstate the market power of food manufacturers since firms should be able to enter these markets more easily than other manufacturing markets.

A further structural consideration is the presence of very strong competition from imported products. In foods with a long shelf-life, this competition is more intense than otherwise because of the ease of transportation and storage.

To summarize my findings on market structure, the processor level seems to be, generally, moderately to highly concentrated. This coincides with the O.F.A.'s analysis of the processor market structure. I now turn to the question of what causes such high levels of concentration; in particular, is discounting a cause?

In fact, it appears that discounting is not the cause. The report of the Commission's consultants, and more specifically the Table reprinted here as Table 13-C, shows

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* Consumer and Corporate Affairs Canada, Working Paper No. 2: Application of Competition Policy to the Food and Agriculture Sector (Bureau of Competition Policy; July, 1978).

TABLE 13-C

SUMMARY OF REBATES OFFERED BY PROCESSORS

(% of processor sales)

Excluding Milk Processors

Sales Volume	On Name Brands	On House Brands	On All Brands
Under $10 million	8.0%	3.2%	7.5%
$10 - $100 million	11.6%	4.3%	11.2%
Over $100 million	9.7%	2.6%	9.0%
Average	10.0%	3.5%	9.5%
Significant difference at 95% confidence level	NO	NO	NO

SOURCE: Processor/manufacturer questionnaire.

that rebate levels do not differ significantly as a percentage of sales for firms of different size when milk processors are excluded. As explained by the consultants, milk processors should be excluded because of their uncharacteristically high rebate levels and over-representation in the middle-sized ($10-$100 million) sales level. Furthermore, applying regression analysis (a statistical measure of correlation between different items) to the processor data received, the consultants find no correlation between the size of firms and rebate levels.

Performance measures of this industry shed further light on conditions in the industry. The performance of the food processing industry, as measured by profits on capital invested, is not satisfactory. Testimony before this Commission and several studies* have highlighted the low and declining profit levels in the processing industries. Poor profit performance can be partly blamed for the continuing demise of participants in this industry as recent examples indicate. In 1978, Christie Brown sold its bakery division to General Bakeries. In 1979, Morrison-Lamonthe sold its bakery division to Corporate Foods. In 1980, the Borden Company sold its dairy division in Ontario to Silverwood Industries.

Again, it is difficult to associate discounting with poor profit performance. Regression analysis of the processor data received by the Commission's consultants

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* The Anti-Inflation Board, _A Study of Profit Margins in the Food Industry_ (Ottawa; 1978), for example.

resulted in the conclusion that there is no evidence of any correlation between rebate levels and return on equity. In fact, the only positive correlation found was between the size of the firm (as measured by sales) and return on equity. The Commission concludes from this evidence that, though the size of the firm and its attendant market power may be an important factor in determining profitability, differences in rebate levels do not explain the variation in profitability between large and small firms. Nor does the variation in the sizes of firms correspond to rebate level differences. Because small processors offer the same level of rebates as larger processors, it is not possible to conclude that discounting is a resolution of market power at the processor level.

While an examination of the causes of low profits experienced by many processors is outside the Commission's terms of reference after the Commission determines that the cause is not discounting behaviour, the following reasons for poor performance have been suggested:

(1) cost increases including cost of ingredients, energy and labour;

(2) import competition; and

(3) low capacity utilization or insufficient economies of scale.

4. CONCENTRATION AT THE WHOLESALER LEVEL

A. GENERAL

Because of the intermediary position of the wholesaler in the food chain, market performance at the wholesaler level will have a direct impact on the viability of other sectors transacting with this level. Small retailers buy large portions of their merchandise through wholesalers rather than directly from manufacturers, and thus depend partially on the wholesaler for success in competing with larger retailers. My examination of the wholesaler sector will begin with market structure and especially with concentration, move to market conduct and end with a discussion of market performance.

The Ontario Federation of Agriculture has contended that the position of small retailers is in jeopardy because of concentration in the wholesale sector. Proper judgment of this contention can only be made upon examination of market conduct and performance measures. More particularly, in view of this Commission's terms of reference, the effect of rebates on concentration in the wholesale sector must be examined.

B. STRUCTURE OF WHOLESALE MARKET

The structure of the Ontario wholesale market shows that the four-firm market share is 51.8%, a level which I have categorized as moderately high. Table 13-D, which also appears as Table 8-B in Chapter 8, sets out the sales

TABLE 13-D

WHOLESALE SALES OF ONTARIO FOOD WHOLESALE FIRMS - 1977

Company	Wholesale Sales ($000,000)	Market Share
M. Loeb Ltd.	581.7	17.63%
The Oshawa Group Ltd.	542.8	16.45%
National Grocers Ltd.	542.8	16.44%
Stuarts Branded Foods Ltd.	41.9	1.27%
Lumsden Brothers Ltd.	40.0	1.21%
UBA Trading Co. Ltd.	34.4	1.04%
Hickson Langs Supply Co. Ltd.	31.0	0.94%
Young-Warren Food Brokerage	25.0	0.76%
Grant Small Sales, Ltd.	24.0	0.73%
Lanzarotta Wholesale Grocers, Limited	20.0	0.73%
Nathaniel Gibbs Canada, Ltd.	20.0	0.61%
Mike's Supermarket 1962, Ltd.	20.0	0.61%
Knechtel Wholesale Grocers Ltd.	18.2	0.55%
Gamble Robinson, Ltd.	15.6	0.47%
Smith and Whittaker Food Brokerage	15.0	0.45%
Elliott Marr and Co. Ltd.	14.8	0.45%
C.B. Powell, Ltd.	14.0	0.42%
H. Fine and Sons Ltd.	13.5	0.41%
Bennett's Foods, Limited	11.6	0.35%
Alex Smith Sales, Inc.	11.0	0.33%
A.S. May and Co. Ltd.	10.0	0.30%
Total of leading 21 firms	1,904.5	
Total Market	3,300.0	

SOURCE: The above figures are estimates derived from: Dun and Bradstreet, 1979 Canadian Key Business Directory amended to agree with published corporate financial reports.

of the twenty-one largest firms operating in Ontario with the major portion of their business in food wholesale. It will be noted that the three largest firms -- Loeb, The Oshawa Group and National Grocers -- are all much larger than their nearest competitors. It should also be noted that this concentration level is comparable to the concentration level in many Canadian manufacturing industries. Finally, it is observed that National Grocers is owned by George Weston Limited, the parent corporation of Loblaws Limited, the province's second largest retailer.

A further structural characteristic which should be highlighted is that most of the full-line grocery wholesalers in Ontario are members of a buying group. Buying groups are treated more fully in Chapter 7. One important function of buying groups is to secure higher volume rebates for their members than the members would receive individually. In fact, ability to achieve higher rebates is partly dependent on membership in a buying group.

Accordingly, the membership requirement of buying groups is a barrier to entry for new wholesale firms where this requirement serves to exclude potential wholesale members. One relatively small wholesaler, Mr. Geoffrey Holt, President of Holt Grocery Distributors Limited, testified that he was unable to comply with a buying group's membership requirements in that his firm did not achieve the required sales volume. In response to this testimony, the General Manager of the buying group involved, Mr. Ralph Moyal of Independent Wholesale Grocers Limited, stated that the group's board of directors establishes certain guide-

lines that prospective members must meet. These guidelines require that prospective members achieve $10 million dollars sales, that they present financial statements for five years, that they possess a warehouse, and that they service more than one retail outlet.

Another buying group, Intersave, consists solely of George Weston Limited subsidiaries and does not appear to be open to companies not affiliated with Weston.

Wholesalers unable to become members of buying groups may be unable to obtain rebate levels achieved by competitors and may be thus at a competitive disadvantage. On the other hand, there are sound business reasons behind membership requirements, especially in view of the group's assumption of financial liability for the member's purchases.

The final point to be made about the structure of the wholesaling sector concerns the buying side of the wholesale market. The wholesaler's customers include retailers of two types. The first type is the independent retailer who has no connection with the wholesaler except that he buys some portion of his groceries from the wholesaler. The second type is the franchised or sponsored retailer who has a preferred position with the wholesaler by virtue of an agreement between the two as described below. The general pattern is that wholesalers sell to retail customers who are much smaller than the wholesalers and who are usually smaller than their retail competitors.

The franchised retailer usually owns his own store and retains profit after all obligations owed to the franchise wholesaler are discharged. However, like a chain store manager, the franchised retailer usually has only a single source of supply which is his franchisor. The retailer is usually required to follow the franchisor's policies in areas such as merchandising, hiring and store layout. The franchisee makes use of the franchisor's services in the areas mentioned above, which include widely dispersed advertising, a superior credit rating (due to the franchisor's signature on loans and leases), and extensive access to new technology.

Table 13-E illustrates the relationship between retail groups and wholesalers. It should be noted that M. Loeb and The Oshawa Group are partners in the IGA franchise. Most relationships illustrated are franchise relationships but some involve a less extensive relationship called, in general terms, "group sponsorship." The group-sponsored retailer uses fewer of the wholesaler's services and exercises more independence as to how his business is operated.

The effect of franchising and sponsorship is that wholesalers are, to a degree, integrated vertically into the food retailing business. By the same token, the retailer may integrate vertically into the food wholesaling business. Once food retailers have grown to a size which would justify support of a warehouse, they begin to buy directly from manufacturers and to perform their own wholesaling functions. The larger chains all perform their own

TABLE 13-E

GROUP SPONSORING WHOLESALERS: ONTARIO OPERATIONS

This table gives the following information about group-sponsoring wholesalers:

Company Name, Central Area of Operation
- Name of retail operations sponsored, number of stores operated.

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Elliott Marr & Co., London
- Superior, 46 stores
- United Buyers, 70 stores

Knechtel Wholesale Grocers, Ltd., Kitchener
- Knechtel Associate Stores, 18 stores
- Knechtel Food Markets, 2 stores
- L&M Food Markets, 8 stores

M. Loeb Ltd., Ottawa, London and Sudbury
- I.G.A., 104 stores
- Muchmore, 33 stores
- Pinto, 87 stores
- Box Stores, 2 stores

Lumsden Brothers, Ltd., Burlington
- Foodland, 17 stores
- Clover Farm, 17 stores
- Best Valu, 160 stores

National Grocers Company Ltd., Headquarters in Toronto, branches across Ontario
- Red and White, 175 stores
- Supersave, 41 stores
- Lucky Dollar, 106 stores
- Maple Leaf, 484 stores
- Marche Suprime, 25 stores
- OK Economy Markets, 2 stores

The Oshawa Group, Ltd., Toronto
- I.G.A., 142 stores
- Ranch, 4 stores
- Food Town and "A" accounts, 100 stores
- Jug City, 17 stores

****

SOURCE: Canadian Grocer, August, 1979

wholesaling and many of the smaller chains perform their own wholesaling as well.

C. MARKET PERFORMANCE

As stated previously, the impact of concentration and integration must be observed in relation to performance measures. In the area of performance, the Commission's consultants found that the wholesalers surveyed operate on net profit margins after tax of less than 1% of sales. The returns on equity for the companies surveyed range between 5.6% and 15.0% with a marked increase in each of the last two years. These figures indicate that concentration in the wholesale market does not allow participating firms to earn higher than normal profits at the present time.

D. MARKET CONDUCT

The Commission's terms of reference demand that I focus my observations about market conduct on the practice of discounting. The Ontario Federation of Agriculture alleged that the buying power of the largest wholesalers produces, through higher rebate levels, increased concentration. The Commission consultants found that the rebate level to all wholesalers is in the range of 5% to 7% of purchases and does not vary significantly with the sales volume of the wholesaler. In finding that there is no signifiant difference in rebate levels between large and small wholesalers, I am unable to conclude that the rebate system favours large as opposed to small wholesalers. Thus, it would appear that the rebate system is not adding to concentration at the wholesaler level.

E. CONCLUSION

In summary, the wholesaler sector is moderately to highly concentrated; more importantly, it is highly concentrated vis à vis the food retailers to which wholesalers sell in most cases. Rebates are not a factor influencing the concentration level; there are no significant differences in rebate levels between large and small wholesalers.

5. CONCENTRATION AT THE RETAILER LEVEL

Certain major participants in this Inquiry expressed a common concern that large retailers in Ontario use their massive buying power to obtain favourable treatment through the mechanism of rebates. More explicitly, the allegation was made that large chains are able to require large rebates and consequently enjoy better net buying prices due to their concentrated and commanding position in the market. This advantage results in increased concentration at the retail level and indeed at all levels of the food industry as alleged in previous sections of this chapter. Because of this advantage and other advantages such as the chain's ability to acquire better site locations than its competitors and the chain's high degree of vertical and horizontal integration, Ontario is in danger of becoming a province like Alberta. It is alleged that independent processors and retailers in Alberta are no longer viable and that only one retailer dominates the industry. All of these concerns will be investigated in this section.

A. ONTARIO RETAIL FOOD MARKET CONCENTRATION

How concentrated is this level of the food industry? To assist in determining the answer to this question, the Commission turned to various measurements of market share. The appropriate market for this Commission's purpose is the provincial retail food market. The reason I confine myself to the provincial market rather than to a local or municipal market is that, when dealing with rebates, retailers and wholesalers buy from processors on at least a provincial basis, if not a regional or national basis. The provincial market share figures provide an indication of relative market strength of the market participants, which in turn allows me to probe the market-power theories that have been advanced.

Statistical data that was presented in testimony by Mr. J. Donald Tigert is reproduced in Table 13-F. The figures in this table represent provincial market-share estimates based on dollar sales. They are derived from company sales figures and Statistics Canada data. In addition, these estimates have been modified by information received by the Commission in its public hearings and by Mr. Tigert's own estimates necessitated by the fact that the companies involved do not release sales figures on a province-wide basis. The Commission found that Mr. Tigert is eminently qualified to advance such estimates and he was widely accepted as an authority in the supermarket industry by other witnesses testifying before the Inquiry.

TABLE 13-F

ONTARIO FOOD STORE MARKET SHARES

Major Chains 1978

Company	No. of Stores	Est. Sales (mil.)	Estimated Market Shares
Dominion Stores			
Dominion	214	$1,392	21.0%
Hiway Market	1	20	0.3
Bittner's	28	28	0.4
Total	243	1,440	21.7
Loblaw Companies			
Loblaw	134	792	11.9
Zehr/Gordon's	52	238	3.6
Ziggy's	10	15	0.2
National Grocers (wholesalers)	NA	395	6.0
Total	NA	1,440	21.7
Steinberg Inc.			
Miracle Mart	79	605	9.1
Valdi Discount Foods	*	*	-
Total	79	605	9.1
Oshawa Group			
Food City	46	241	3.6
Dutch Boy	8	30	0.5
IGA Wholesale	NA	210	3.1
Total	NA	481	7.2
A & P	99	400	6.0
M. Loeb Limited			
IGA Wholesale	NA		
Pinto Stores	NA		
Total	NA	400	6.0
Canada Safeway	36	180	2.7
Becker Milk	586	152	2.3
Mac's Milk	406	117	1.8
All other Food Stores	NA	1,429	21.5
GRAND TOTAL	NA	$6,644	100.0%

NOTE: * new division in 1979.

SOURCE: Estimates by J. Donald Tigert, Burns Fry Limited

Statistical data from the trade publication _Canadian Grocer_ was also presented to the Commission and is reproduced in Table 13-G. These estimates, like Mr. Tigert's estimates, are based on company sales figures and Statistics Canada data. They also include estimates by the publication's staff.

Statistical data from the market-service publication _National Market Development Grocery Guide_ was also presented as evidence to the Commission. This data is not reproduced here because it reports percentages of shopping trips, not of dollar values which are more pertinent to the determination of buying-power questions.

The Commission acknowledges that these food store market-share estimations neglect the role played by restaurants, fast-food outlets, drug stores, department stores and other institutions engaged in the sale and purchase of food in Ontario. It is further acknowledged that the sale of non-food items in the modern supermarket may overstate the sales of the chains which sell more of these types of goods than other outlets. Nevertheless, these estimations and particularly those of Mr. Tigert, provide a useful, if limited, starting point for discussing concentration in the industry and especially for assessing the validity of the independent store as competitor of the chain store.

From the two tables presented here, it is observed that the top four firms have a market share slightly in excess of 50%, a share which I identified as moderately high

TABLE 13-G

ONTARIO FOOD STORE MARKET SHARES

	No. of Stores	Share of Ontario Food Sales (%)
Loblaws	139	12.9
Zehrs/Gordons	37/15	2.4
Dominion	221	25.6
Miracle Food Mart	67	9.1
A & P	98	6.2
Canadian Safeway	45	2.1
Becker's	26	2.5
Mac's	580	1.9
Other Chains	410	3.9
Total chains' share (Ontario)		71.9
INDEPENDENTS		
Voluntary Groups (Loeb, National, Oshawa, etc.)		17.9
Unaffiliated		10.2
		100.0%

SOURCE: Estimates based on various sources including company sales figures, Canadian Grocer's annual Food Broker issue and Market Study (February 1978) and Statistic Canada. Table 13-G represents percentage for all Ontario, not just major market areas which tend to amplify chains with metropolitan concentrations of either store numbers or store sizes.

in discussing the processor and wholesaler sectors of the industry. The significance of this finding is that the top four firms in the retail sector are, in fact, in a powerful market position vis à vis many food suppliers, but not all. A food supplier who is unsuccessful in selling his product to Dominion Stores, Loblaw Companies, Steinberg/Miracle Mart and A&P will not gain access to half the consumer dollars spent in food stores in this province.

The six major chains in Ontario -- Dominion Stores, Loblaws, Steinberg/Miracle Mart, A&P, Safeway, Oshawa/Food City -- will be familiar to many, if not all, of our readers. Their operations are not limited to Ontario as they have established a major presence in almost all the Canadian provinces, although not all six are present in each province. They are discussed individually more fully in Chapter 9 on retailers.

The discussion in Chapter 9 will be recapitulated briefly here. The number of stores in Ontario ranges from Canada Safeway's 36 to Dominion Stores' 220 stores. These stores are generally larger than the stores of competitors, though not always. The major chains are the most vertically integrated of Ontario food retailers, conducting many of their own manufacturing and processing operations as will be explained in the section dealing with this topic. The major chains are often located at superior sites in metropolitan areas and suburban shopping centres, a topic which will also be dealt with more fully in a later section of this chapter.

Deducting the major chains' share of the Ontario retail food market, we find that the remaining share is held by an amalgam of types of retailers which is loosely referred to here as Ontario's "minor retail food chains and independents." These will be identified as follows:

(1) minor combination chains

(2) major and minor convenience chains

(3) franchised and voluntary group independents

(4) unaffiliated combination independents

(5) unaffiliated convenience independents

(6) specialty chains

(7) specialty independents

These terms will be explained as I describe the types. This description is essentially the same as the one found in Chapter 10, Small Retailers and Rebates. The reader who has read that chapter, in other words, need not read what follows.

1. Minor Combination Chain

The first type within this amalgam is the minor combination chain. Minor chains such as Knob Hill Farms (five stores) and Calbeck's (six stores) differ from the major chains in that the minor chain's stores are generally located in a region rather than province-wide and in that these chains are not vertically integrated to a significant degree. The minor chains are like the major chains in that they purchase most, if not all, of their merchandise directly from suppliers. However, most, if not all, minor chains are members of buying groups whereas only two of the

major chains (Loblaws and A&P) are members of such groups. The minor combination chain store usually has as much selling space as the major combination chain store and sells the same full line of commodities.

2. Major and Minor Convenience Chains

The second type within this group is the major and minor convenience chains. Stores within these chains again may be operated on a franchise basis but not always: Mac's Convenience Stores Limited, for example, franchises its stores, while the Becker Company owns most of its stores. The convenience store ranges in size from 600 to 2,400 square feet and carries a limited line of products, usually eliminating fresh meat but emphasizing tobacco products and milk. These stores are called "convenience" stores because they generally offer consumers proximity, later hours on week nights and weekends, and shorter lineups; these are privileges for which the consumer must often pay a premium in the form of higher prices. In addition to the major chains, Mac's and Becker's, Ontario has many convenience store chains whose sales are less important, among which are Pinto Stores (an M. Loeb franchise), Seven-Eleven (a chain based in the United States), and Jug City (an Oshawa Group franchise).

3. Franchised and Voluntary Group Independents

The third type within this group is the franchised and voluntary group independents. As explained in the wholesaler section, the franchised independent store, often

franchised to one of Ontario's three largest wholesalers, resembles the independent store in that the franchised store owner invests his own funds and retains whatever profits the store earns over and above whatever debts the owner may owe. However, the sales of these independents are often represented as the sales of a chain (see Table 13-F), or as the sales of the wholesaler (see Table 13-G). This classification reflects the close resemblance that a franchised store bears to the chain store in that the franchisee usually must sell the franchisor's products at a price established by the franchisor, and adhere to the franchisor's merchandising policies. The independent who is a member of a voluntary group is related to his wholesaler in much the same way as the franchisee, as explained earlier.

4. Unaffiliated Combination Independent

The fourth type is the unaffiliated combination independent. The unaffiliated independent may deal directly with some suppliers, but it buys most dry groceries -- breakfast cereals, canned and frozen fruits and vegetables, biscuits and many other items -- from wholesalers. The unaffiliated independent does not necessarily buy from only one wholesaler, although the fact that only one or two wholesalers compete in his area may effectively limit the unaffiliated independent's choice. In major metropolitan areas like Toronto or Hamilton, however, the independent's choice of a wholesaler is much wider. The wholesaler that the unaffiliated independent patronizes often belongs to a buying group.

5. Unaffiliated Convenience Independent

The fifth type is the unaffiliated convenience independent. These stores usually measure less than 7,000 square feet and often are referred to as the "ma-pa" store, reflecting the fact that these stores are often family-owned and family-operated. These stores are also frequently referred to as "corner stores" reflecting their location, but it should be noted that this appellation may refer, as well, to the chain convenience store. However, the chain convenience store often has the advantage of connection with a dairy, as in the case of Mac's and Becker's, for example, or with the wholesaler, as in the case of Pinto and Jug City stores, for example. This advantage sets it apart from the unaffiliated independent.

6. and 7. Specialty Chains and Independents

Yet another type within the group is the specialty store: the local butcher and baker, as well as the local fruit and vegetable grocer, are examples. These stores, too, may be organized into chains which have diversified into products other than the specialty. Ziggy's, known primarily for meat products, is an example of a specialty chain; this chain happens to be affiliated with Loblaws Limited and the Weston empire.

I have now identified two major groupings of food retailers: (1) major chains, and (2) minor chains and independents.

Concern has been expressed as to the future viability of the second grouping. Mr. Kenneth Gadd, General Manager of the Canadian Federation of Retail Grocers, whose membership encompasses a variety of food retailers nation-wide, expressed the concern that the status of independent grocers in Ontario is deteriorating when he testified, "...he is an endangered species. Not to the point of elimination, but certainly to the point of a reduction in numbers which will present a position not particularly favourable to the Canadian economy."

Is this concern justified? Is the independent grocer an endangered species whose numbers are being constantly reduced? An examination of historical trends in market share statistics will give us some indication as to the current status of Ontario's independent grocer. Table 13-H represents an estimate of sales figures for eleven years based on Statistics Canada figures with adjustments made by _Canadian Grocer_'s staff based on their information and knowledge of the industry.

Before I analyse these figures, a word should be said about the definitions of the terms used since these definitions affect the analysis. First, the term "chain" is based on Statistics Canada's definition of a "chain store organization" being four or more stores under single ownership. Therefore, the "chains' share" provided in the Table will include sales figures of the minor chains such as Knob Hill and Calbeck's. Also included are sales figures of the convenience chains: those of the major convenience chains, Mac's and Becker's, in addition to those of the minor

TABLE 13-H

DISTRIBUTION OF ONTARIO FOOD SALES

1969 - 1979

		Total Independents	
	Chains' Share	Group Independents	Unaffiliated Independents
1969	61.2%	23.1%	15.7%
1970	63.1	21.4	15.5
1971	64.4	19.7	15.9
1972	69.8	15.8	14.4
1973	70.7	16.8	12.5
1974	72.2	17.6	10.2
1975	72.2	17.7	10.1
1976	70.8	18.5	10.7
1977	72.4	17.6	10.0
1978	73.1	17.2	9.7
1979	73.8	16.8	9.4

SOURCE: Estimates from Canadian Grocer, February 1980

chains. The minor chains include chains such as Scarborough Fair which has only ten stores. Thus, the "chains' share" estimate includes more than the share of what I have identified as the major combination chains.

Second, the term "group independent" refers to what I have called "franchise and voluntary group independents": that is, those retailers who have a special relationship to a wholesaler. The wholesaler that these retailers are related to is often one of the three largest wholesalers in Ontario.

Third, the term "unaffiliated independents" refers to "unaffiliated combination independents" and "unaffiliated convenience independents." It does not include what I have termed "specialty independents." In fact, specialty-food sales are not represented in these estimates.

What these figures from Canadian Grocer illustrate is that the chains' share, as defined above, has indeed increased during the eleven-year period 1969 to 1979 by 12.6%. During the same period, the share of all independents has decreased by that amount apportioned equally between group independents and unaffiliated independents. As mentioned, however, this decrease is somewhat mitigated by the fact that the "chains' share" includes some of the minor chains. Thus, a firm like Knob Hill Farms which expanded to over three stores during this period, had its sales reclassified from the "unaffiliated independent" category to the "chain" category by the very fact of its success. The Canadian Grocer figures also indicate that

the chains' rise is not nearly so pronounced over the second half of the period as it is over the first half; in fact, the chains' share rose only 1.6% from 1974 to 1979, compared to 12.6% during the entire period.

The same trend is identifiable in the figures provided the Commission by respected food industry analyst J. Donald Tigert, based on data presented in a publication of Statistics Canada. These figures are reproduced in Table 13-I. This table indicates that while the proportionate market share of unaffiliated combination independents (including unaffiliated combination independents and franchised and voluntary group independents) has decreased from 1974 to 1979 by .2%, the total sales of the same group have, in fact, increased by $353 million, or 66%. Similarly, while the proportionate market share of independent grocery and confectionary stores and other stores (including unaffiliated convenience independents and specialty independents) has decreased over this period by 1.7%, total sales for these classifications have increased by $292 million, or, in percentage terms, by 72%. It is also worthy of note that the number of retail food stores in Ontario has increased 32.3% over the period 1975 to 1978 according to the estimate of Canadian Grocer (February, 1979).

This data allows us to draw the tentative conclusion that, although the major and minor chain stores have rapidly increased their market share during the last ten years at the expense of the independents, this increase has markedly slowed since 1974. Furthermore, the shift in market share does not translate into less sales for the

TABLE 13-I

DISTRIBUTION OF ONTARIO FOOD SALES 1974 - 1978

Combination Stores (1)	1974	1975	1976	1977	1978
Chains	$2,642	$3,072	$3,370	$3,710	$4,193
Independents	688	800	871	920	1,041
Total	$3,330	$3,872	$4,241	$4,630	$5,234
Grocery & Confectionery Stores (2)					
Chains	186	232	248	274	312
Independents	403	474	624	599	618
Total	589	706	872	873	930
All Other Food Stores(3)					
Chains	64	55	59	61	65
Independents	338	353	407	376	415
Total	402	408	466	437	480
Total Market					
Chains	2,892	3,359	3,677	4,045	4,570
Independents	1,429	1,627	1,902	1,895	2,074
Total	4,321	4,986	5,579	5,940	6,644
Market Shares					
Combination Chains	61.1%	61.6%	60.4%	62.5%	63.1%
Combination Independent	15.9	16.0	15.6	15.5	15.7
Other Chains	5.8	5.8	5.5	5.6	5.7
Other Independent	17.2	16.6	18.5	16.4	15.5
Total Market	100.0%	100.0%	100.0%	100.0%	100.0%

NOTE: 1. Combination Stores - grocery stores with 20% or more fresh meat (includes supermarkets of the type operated by Dominion, Loblaws, Miracle Mart, IGA and Knob Hill Farms).

TABLE 13-I

DISTRIBUTION OF ONTARIO FOOD SALES 1974 - 1978
(continued)

NOTE: 2. Grocery, confectionery & sundries store - grocery stores with 20% or less fresh meat (includes "jug milk" and "convenience" stores of the type operated by Becker's and Mac's Milk.

3. All other food stores - bakery product stores; candy, nut and confectionery stores; dairy product stores; egg and poultry stores; fruit and vegetable stores; meat markets; fish markets; delicatessen stores (includes stores such as Bittner's, Fruit fair, Laura Secord, Woman's Bakery).

SOURCE: Retail Trade in Canada, Statistics Canada, Catalogue No. 63-005, submitted by J. Donald Tigert

independent category; on the contrary, independents have enjoyed an increasing sales total not entirely explained by inflation.

The rapid rise in the Ontario food-chain market share between 1969 and 1979 coincides with a prolonged national trend in food retailing. The 1935 Royal Commission on Price Spreads, likewise relying on Statistics Canada data,* reported that the combination chain stores held 33.2% of the market in 1933. This figure had risen by only 6.4% in twenty-two years to 39.6% in 1955, as reported three years later in a study on price discrimination in the grocery trade commissioned by the federal Restrictive Trade Practices Commission. The chains' share rose by 6.3% over the next twelve years to 45.9% as reported by the Canadian Grocer in 1967, but rose sharply by 14.3% over the next eleven years to 60.2% in 1978, as reported in the same publication. However, the pace of increase relents nationally as it does provincially: the chains' share rose only 0.4% from 59.8% to 60.2% during the period 1974 to 1978.

B. CAUSES OF ONTARIO RETAIL FOOD MARKET CONCENTRATION

What factors have enabled the chains to sustain this growth in market share over the last forty-five years?

* Since 1935, Statistics Canada definitions have changed; for example, the amount of meat a store must sell to qualify as a "combination" rather than a "grocery" store has been varied. Again, this Commission is using these figures to gain a rough, rather than exact, appreciation of trends in the industry. Also, this is the best data available to the Commission.

What factors have enabled the independents to halt deterioration of their market share over the last five years? I will study these questions in subsequent sections numbered as follows:

1. vertical and horizontal integration
2. site location
3. economies of scale
4. the Alberta situation

1. VERTICAL AND HORIZONTAL INTEGRATION

One of the features differentiating the major combination chains from the other groups of Ontario food retailers is the former's marked degree of vertical and horizontal integration. The major chains are the owners of interests in competitors at their own level and in suppliers at other levels at the food chain. There is also a degree of vertical integration in that important wholesalers and suppliers are legally affiliated with retailers.

An organization chart for George Weston Limited, is provided as Table 13-J. Not only does the so-called "Weston Empire" include the 132-store Loblaws Limited chain, but it also includes National Grocers, one of the three leading wholesale firms in Ontario. National Grocers franchises and sponsors as voluntary groups six "chains" of independents which in total account for approximately 833 combination and grocery convenience stores. Zehr's Markets and Gordon's Supermarkets, both Loblaws subsidiaries, operate substantial retail chains in the Kitchener and Windsor areas respectively. Ziggy's Fast Foods is a specialty

GEORGE WESTON LIMITED
ORGANIZATION CHART

Food Processing

Bakery

- \- Weston Bakeries Limited 100
  - Lane's Bakeries Limited 100
- \- McCarthy Milling Limited 100
- \- Soo Line Mills (1969) Limited 100

Biscuit

- \- Interbake Foods Limited 100
- \- McCormick's Limited 100
  - Imperial Cone Company
- \- Paulin Chambers Company Limited 100
- \- Weston Foods Limited 100

Chocolate & Dairy

- \- William Neilson Limited 100
- \- Donlands Dairy Company Limited 100
- \- Clark Dairy Limited 99

Food Specialities

- \- Bowes Company Limited 100
- \- Chocolate Products Company Limited 100
- \- McNair Products Company Limited 100
- \- Rose & Laflamme Company Limited 100
- \- Watt & Scott Incorporated 100
- \- Westcane Sugar Limited 100
- \- Niagara Food Products Company Limited 100

Fisheries

- \- British Columbia Packers Limited 83
  - B.C. Packers (Quebec) Limited 100
  - McCallum Sales Limited 100
  - Nelbro Packing Company 100
- \- Connors Brothers, Limited 97
  - H.W. Welch
  - Lewis Connors & Sons

Retailing & Wholesaling

- \- Loblaw Companies Limited 87
  - Kelly, Douglas & Company Limited 84
    - Fairview Farms Limited 100
    - Foremost Foods Limited 100
    - Kingsway Frozen Foods
    - W.H. Malkin Limited 100
    - Meteor Meat Company Ltd. 100
    - R.E. Sang Limited 100
    - Weston Commodities Ltd. 100
    - Westfair Foods Limited 100
      - Dominion Fruit
      - Econo-Mart
      - Loblaws
      - O.K. Economy Stores
      - Shelly Western
      - Shop Easy
      - Tom Boy
      - Western Grocers
  - Loblaws Limited 99
    - Atlantic Wholesalers
    - National Grocers Company Limited 100
      - Lucky Dollar Food Stores
      - Maple Leaf Food Stores
      - O.K. Economy Markets
      - Red & White Food Master
      - Super Save Markets
    - Zehrmart Limited 100
      - Gordon's Super Markets
      - Zehr's Markets
    - Ziggy's Fast Foods
  - Z & W Foods Limited 67

NOTE: 1. Table shows % of common or participating shares owned by indicated parent company, May 31st, 1979. Companies in furthest left position in each column and with a "-" before their names are owned by George Weston Limited. Other companies are owned by the company under which their names are indented. Chart represents Canadian operations only.

chain operated as a division of Loblaws Limited. The above-mentioned are simply the Ontario-based wholesaling and retailing operations of George Weston Limited; other Weston interests include a major Western Canada wholesaler and a major retail chain in the Maritimes. The latter interest owns the Ontario wholesaler, Lumsden Brothers, to which the Clover Farms and Foodland retail outlets in Ontario are franchised.

The above wholesale and retail operations are affiliated through common corporate ownership with some of Canada's major food processors. Weston Bakeries Limited is further vertically integrated due to Weston Limited's ownership of two flour milling businesses. Weston's five biscuit processors also benefit from this relationship. Milk processors owned include Donlands Dairy Company, one of the four largest dairies in Ontario, and Clark Dairy, a major force in the Ottawa area. Neilson, the well-known ice cream and confectionery manufacturer, is another wholly-owned subsidiary. Other subsidiaries include West Cane Sugar Limited, one of Canada's six sugar refineries which together control 100% of that market; Bowes Company, a nut and dried fruit importer/trader; and Connors Brothers, claimed to be the largest sardine packer in the world by the President of Loblaws Ltd.

In 1979, George Weston Limited attempted unsuccessfully to acquire control of the major Ontario retailer, R. Simpson Company Limited. The importance of other retail holdings such as department store businesses will become clear when the issue of site location is discussed.

An organization chart for Dominion Stores Limited is provided as Figure 13-A. The vertical and horizontal integration of Dominion Stores Limited is not as extensive as that of the Weston Empire, but it is still substantial. The 220-store Dominion Store chain, owned by the powerful Argus corporation, is affiliated through a holding company, Quintana Incorporated, with a number of other retail outlets. These include Kitchener's Hiway Market, two chains of limited-line "box" stores, a convenience-store chain, a gas-bar chain and a drug-store chain. The 26-store Bittner's Stores Limited chain sells a limited line of meat and delicatessen items supplied by the meat processor and sister-subsidiary Bittner Packers Limited.

Dominion Stores Limited is affiliated with other processors as well as Bittner Packers. The company owns 56.5% of the shares of General Bakeries Limited which purchased the bread division of one of its major competitors, Christie Brown, in 1978. Through Quintana, Dominion Stores is affiliated with Parkway Wholesale Limited which conducts food wholesaling and distributing in the Kitchener area. Dominion Stores also has interests in wholesalers and distributors in the Maritimes. Though Dominion Stores has no ownership interest in farms, the well-known manufacturer of farm machinery, Massey-Ferguson, is an Argus subsidiary.

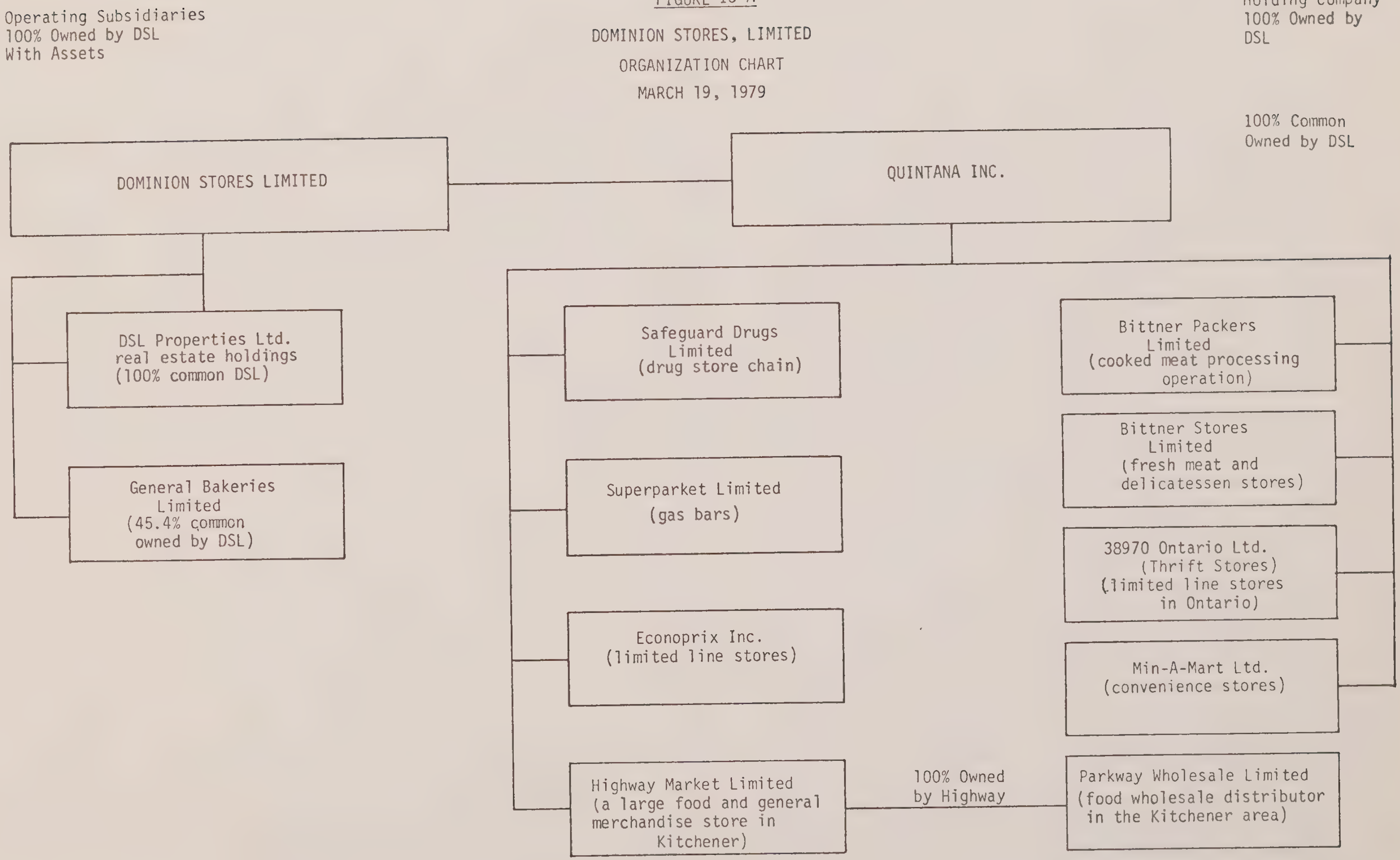
Steinberg Incorporated operates 69 stores in its Ontario division known to consumers as Miracle Food Mart. The company operates another ten stores in the Ottawa area through its Quebec division. Steinberg's owns the limited-line box store chain Valdi Discount Foods, in addition to

FIGURE 13-A

DOMINION STORES, LIMITED

ORGANIZATION CHART

MARCH 19, 1979



restaurants and fast foot outlets. The Miracle Mart division operates a number of department stores.

Steinberg, like George Weston Limited, owns one of Canada's major sugar refineries, Cartier Sugar Limited. It also processes baked goods with flour obtained from its own mill. Steinberg Foods Limited, a subsidiary corporation, manufactures bakery and delicatessen items in addition to packaging tea and coffee. Steinberg Foods also distributes products manufactured by its subsidiary Multimarques Incorporated, including frozen pizza pie, nuts, confections, wieners and sausages.

The Great Atlantic and Pacific Company of Canada, Limited ("A&P") was recently purchased by TN Delaware Incorporated which is in turn wholly owned by a major West German food retailer. A&P Drug Mart is a separate merchandising company operating one drug store and two in-store pharmacies. A&P operates a chain of 99 stores in Ontario and is affiliated with the frozen-food processor Metcalfe Foods and the Jane Parker Bakery.

The American company, Safeway Stores Incorporated, owns all but a small number of the shares of Canada Safeway Limited which operates 26 southern Ontario stores in its Toronto zone. Canada Safeway also operates ten more northern Ontario stores in its Winnipeg zone in addition to operating stores in its western operation. Safeway is a much stronger force in the western retail food market than in Ontario, as will be explained in the section on the

Alberta situation. The company owns a milk processor, and bakery and canning operations. It also owns its own wholesale and warehousing firm.

Vertical and horizontal integration links are not restricted to Ontario's major chains. Such links are an advantage enjoyed by other groups in the food industry as well. The wholesalers Oshawa Group and Loeb, and also the major convenience chains Becker's and Mac's, are vertically integrated to a considerable degree.

The Oshawa Group Limited is one of the three major wholesaling firms discussed in the previous section. However, since Oshawa's acquisition of the Independent Grocers Alliance (IGA) franchise in 1951, Oshawa has been an important force in the retail market as well. Oshawa is the franchisor of 137 IGA stores and owns sixteen more IGA stores.

Pursuant to a partnership agreement with M. Loeb Limited of Ottawa and the H.Y. Louie Company Limited of Vancouver, Oshawa supplies IGA franchisees in south-central Ontario while Loeb supplies IGA stores elsewhere in Ontario. In addition, Oshawa owns 45 Food City stores and operates the five-store Dutch Boy, and the three-store Dutch Girl, chains as one division. It also sponsors the ninety-five store Food Town and five-store Ranch chains in addition to sponsoring the seventeen-store Jug City convenience stores. Oshawa also has an interest in Towers Department Stores.

The major shareholder in M. Loeb Limited is Provigo Incorporated of Montreal, one of the leaders in the Quebec convenience store retail food market. As a wholesaler, Loeb supplies over 2,000 food stores in Ontario. As a franchisor of retailers, Loeb's partnership in IGA gives Loeb the franchise for 105 stores in eastern, northern and south-western Ontario. Loeb also franchises the 102-store Pinto convenience chain. A wholly owned subsidiary of Loeb's conducts franchise operations in the west. Finally, Loeb owns the Capitol Transport Company which does all of Loeb's hauling plus that of other companies.

The Becker Milk Company franchises 580 convenience stores between Ottawa and London. The milk and ice-cream products carried by Becker Stores are exclusively manufactured by the Becker Company's dairy. The other major convenience store chain in Ontario, Mac's Convenience Store Limited, is a wholly owned subsidiary of Silverwood Industries Limited, as is Silverwood's Dairies. Mac's franchises 410 stores between Ottawa, Windsor, Sarnia and Sudbury.

These are the vertical and horizontal integration links that have come to my attention. Some retail companies are affiliated with other business which assist them in carrying on operations such as packaging and transportation. It is obvious merely from the affiliations listed that vertical and horizontal integration is a prevalent feature of the Ontario food industry.

Vertical and horizontal integration are aspects of structure which may affect conduct and performance. Both

types of integration may create a barrier to entry for potential new firms if the cost and availability of supplies prohibit the new firms from competing with the integrated company. Horizontal integration, by definition, increases the market share of the merging companies. This should directly increase the buying power of the merged company to the disadvantage of potential entrants which deal with and compete with the company.

Horizontal integration may increase the efficiency of the integrated firm if economies of scale can be realized. On the other hand, the integration of competing firms may simply eliminate a competitor, leaving the integrated firm with less incentive to be efficient. Horizontal integration may also have a detrimental effect on competitors at the same level who are unable to match the merged company's buying power and selling price.

Vertical integration may save the consumer money in that certain costs are avoided when one firm sells product to a firm that it owns: sales-force expenditures, for example, need not be incurred. Integration between food retailers and their suppliers, however, may have a detrimental effect on competition if competing suppliers are thereby excluded from the retailer's shelf without consideration given to the merits of the competing product's quality and price.

2. SITE LOCATION

The ability of the chain to secure better site locations was repeatedly offered by various witnesses as a response to why the retail food sector in Ontario is as concentrated as it is. The Ontario Federation of Agriculture cites examples of suburban and rural shopping centres which draw shopping traffic away from small towns and small cities. The O.F.A. warns in its brief that the pervasive expansion of the chains to small-town and small-city Ontario "represents a direct challenge of the chains to the remaining market share of the independent grocer."

The President of M. Loeb Limited, Mr. Frank Warnock, also voiced similar concerns with respect to his company's retail franchises. Mr. Warnock raised what he considered to be the ominous prospect of the Weston Empire virtually filling a given shopping centre should it have succeeded in its recent proposed takeover of a major Ontario department store chain.

The importance of shopping centres to the revenues of Canadian retailers was documented as long ago as the 1935 Report of the Royal Commission on Price Spreads. Shopping centres offer consumers the advantage of free parking and one-stop shopping for a variety of goods. As a result, and depending on the centre's proximity to urban populations, a lease in a shopping-centre development is highly desirable to food retailers.

At the same time, choice of a supermarket tenant is very important to the developer of a shopping centre. The developer wants a food retailer whose name is known well enough to draw the largest number of customers possible to a particular centre. The developer also wants a tenant who is a solid credit risk in order to better secure further financing for the project. Finally, the food chain's affiliation with a drug store or other type of retailer might offer the developer the opportunity of "killing two birds with one stone" by negotiating with one company. These preferences usually not only dictate the choosing of a chain supermarket rather than an independent, but also give the chain leverage in its negotiations with the developer.

In negotiations, the chain might exact from the developer a covenant that would restrict the developer from leasing space to a competing food retailer, not merely within the confines of the particular centre but even extending over a radius of one or two miles. This restriction may be perpetrated for a twenty-year period, or longer, depending on renewal-option clauses in the lease agreement.

The issue of site location is only critical to findings of this Commission if a connection is established between concentration and discounting. The Commission has not established any links between site location and discounting. For these reasons, the Commission is reluctant to express an opinion about the issue of site location.

Proposals for legislation directed against the attempts of chain retailers to obtain prime shopping centre locations, or against the disbursement of development-assistance funds by the Ontario Government, would certainly be rash without considering the interest of developers in obtaining the best possible tenants. An indirect result of such legislation may be to deprive small towns and small cities in Ontario of the competition that chain stores could offer.

Finally, the remark should be made that shopping centre location might be a problem which will take care of itself. Energy shortages may make travel to such suburban sites less attractive as opposed to existing downtown sites, sites that are usually controlled by developers to a lesser degree.

3. ECONOMIES OF SCALE

The major chains enjoy economies of scale which enable them to save costs, other than economies that they derive from integration. One of the most significant cost-savings is due to economies of local advertising.

Economies of local advertising refer to the economies involved where a firm can place an advertisement pertaining to several stores in the area of the advertisement. Suppose one firm receives revenues from 30 stores in a given municipality. Suppose further that this firm pays media with city-wide distribution the price of one advertisement effective for all 30 stores. Such a firm clearly has an

advantage over the firm that must pay for the same space with revenues from only one, two or three store(s). From the standpoint of advertising, therefore, a retail firm is wise to proliferate stores in an urban market. Conversely, the market entrant with few stores may find it difficult to compete with the colourful and expensive advertising which the major chain is able to distribute within the entrant's market area.

There are also purchasing and delivery economies arising from the purchase of full truckloads of commodities. Such truckloads are brought into large warehouses or large stores which are fully mechanized in order to handle the delivery efficiently and expeditiously.

The stores and head office of a major chain may also realize economies of scale. They can effectively compartmentalize the work that must be performed so that staff learn and become proficient at special tasks.

The major chain's investment capabilities are such that it can afford high-priced technological improvements. One example of technological improvement is the computerized scanner which may revolutionize grocery store checkout procedures.

The chain's superior number of employees and financial capacity make it easier for the chain than for the independent to adapt to changes in government policy such as the federal government's recent efforts at conversion to the metric system. The minimum-delivery requirements of

certain suppliers are easily met by major chains, but not so easily met by independents who cannot afford to tie up funds in inventory.

Credit difficulties and generally fewer financial resources also hinder the the minor chains and independents from participating in so-called "price wars." In 1973, for example, the price of milk along with the prices of other staples such as eggs, bread and sugar, were forced to such low retail levels that complaints about declining profits were voiced even by the chains. Such a "war" is particularly difficult for smaller outlets that depend heavily on staple products.

4. THE ALBERTA SITUATION

The competitive situation of another province became a topic of concern before this Commission. This concern was prompted by the warning sounded in the Report of the Standing Resources Development Committee that Ontario "could be following the unfortunate example of Alberta." In that province, it is alleged, one chain (Canada Safeway) dominates the grocery market.

Each of the advantages described above has an impact in the context of the Alberta situation. This section is a discussion of a concentrated market, rather than a discussion of a cause of concentration. Safeway's "stranglehold position" in Alberta is fortified by vertical integration into trucking, dairy, canning, and grocery-wholesaling operations. In addition, Safeway is said to dominate the

superior site locations. This makes it difficult for his company to secure products and site locations in the west, alleged Mr. Frank Warnock, president of M. Loeb Limited, one of the partners in the IGA franchise which competes with Safeway in Alberta. The same witness suggested that the Safeway experience in Alberta could be duplicated in Ontario by an oligopoly of three companies rather than a monopoly of one.

In 1973, proceedings pursuant to the Combines Investigation Act were commenced against Canada Safeway. The proceedings alleged that the company was a party to a monopoly in that it substantially controlled the business of operating retail grocery stores in the cities of Calgary and Edmonton, Alberta, to the detriment or against the interest of competitors. To avoid lengthy and very expensive litigation, Safeway consented to the terms of two orders. These two orders, in essence, prohibited the company from: (1) meeting or undercutting the price of a competitor in Calgary unless the price was applied uniformly to identical items sold in all its Calgary stores, (2) increasing the total square footage occupied by its stores and opening more than one new store per year in each of the two cities, (3) entering into restrictive clauses or covenants in leasing arrangements, (4) acquiring existing grocery stores for five years, and (5) engaging in market-saturating advertising policies.

It should be noted that in consenting to the orders, Safeway did not admit that any offence had been committed by it. On the other hand, the prosecution admitted to

encountering unforeseen evidence establishing that the company's market share, an essential element for establishing guilt in a monopoly prosecution, was not of the magnitude that it was believed to be before the prosecution was commenced.

The Director of Investigation and Research under the Combines Investigation Act testified, before this Commission, that Canada Safeway has fully complied with the terms of the consent order to the satisfaction of his office. As to whether the order was effective in reducing the degree of concentration in the two markets involved, the Director pointed out that such an evaluation was impossible to make without knowing what would have happened had the order not been in effect. Nevertheless, in the Director's opinion, the order did have a restraining effect on concentration in the Calgary and Edmonton markets.

This Commission is unable to determine precisely what state of competition exists today in the Alberta retail food market, though it can be stated with certainty that Safeway has a strong if not dominant position in both the Edmonton and Calgary markets.

Evidence was given by Mr. Tigert that Safeway's degree of control in the west permits the company to earn higher pre-tax profit margins than Dominion Stores, which retails predominantly in the east. This is so even though Dominion Stores appears to be more efficient as indicated by its better ratio of sales per square foot compared to Safeway's. (Safeway reports profit figures on a consolidated

basis including its processing concerns so that this cannot be stated with certainty, Mr. Tigert pointed out.)

The testimony of Mr. Brian Robert Waring, the Grocery Products Manager of St. Lawrence Starch Limited, an important force in the manufacture of corn oils and syrups, supports Mr. Tigert's opinion. Mr. Waring testified that, in his words, "you have principally one major chain west of Winnipeg, Safeway....There is certainly no where near as much (competition) there as there is here in Ontario." The effect is, according to this witness, that the competition obliges retailers to pass through to consumers the discounts offered them by suppliers "nine times out of ten" in Ontario; in any event, more often than in the west.

What role does discounting play in assisting Safeway to achieve and maintain the competitive position which it holds in the Alberta market? It is worthy of note that none of the court documents filed in the 1972 Combines case referred to the practice of discounting. The Safeway representatives themselves testified under oath before my Commission that discounts and allowances paid to Safeway are the same in percentage terms east or west of Winnipeg; as mentioned, many of Canada's retailers and suppliers market their products in both halves of the country. The Chairman of the Board and President of A&P, Mr. Kennedy, attributed his company's inability to compete in the west not to discounting but to failures in A&P's merchandising program.

In short, though many causes may be attributed to Canada Safeway's achievement of an alleged monopoly position in the west -- including Safeway's ability to secure superior site locations and its high degree of vertical integration -- discounting does not appear to be one of those causes.

As for the allegation that Ontario is following Alberta's "unfortunate example," any tendency towards the domination of one food chain or even of two or three chains in the Ontario market was vehemently denied by many participants in this market. It is not merely Dominion Stores, Loblaws and Steinberg/Miracle Food Mart which expressed confidence in their ability to compete, but also many other chains and independents which, though they may have less sales now, consider themselves capable of providing the three major chains with viable and strong competition for many years to come.

The Commission finds that the confidence of such corporations as A&P, The Oshawa Group, M. Loeb Limited and Canada Safeway itself, is certainly well-founded confidence. The claims of the other competitors must now be examined.

C. THE FUTURE OF THE INDEPENDENT RETAILER

I have now outlined an answer as to why the major chains have been able to capture a large share of the retail food market over the last 45 years. The question remains as to what factors have enabled the independents to

halt deterioration of their share of market over the last five years? Is this resurgence only temporary or can Ontario's minor chains and independents reasonably hope to retain their important status in the future?

Consumers shopping in an independent store have the advantage of patronizing an in-store owner whose livelihood depends on the success of his investment. This often translates into a more personalized atmosphere extending to services -- home delivery, cheque cashing, carry out, credit and other services -- which are not the chains' usual business practices. The in-store owner may also be able to exert more control over employees. He can often be more flexible in meeting or introducing lower prices since the chain store must usually wait for the weekly directives from head office. And because his head office is not located in another region, the in-store owner is often in better touch with the merchandise preferences and needs of the local patron.

The minor chains and independents are generally not unionized. The importance of this is illustrated by the evidence of representatives of Becker's and Mac's that employees of their franchised managers generally receive three to four dollars per hour in comparison to the eight to nine dollars paid to comparable labour in chain stores. Absence of a collective-bargaining agreement also means that minor chains and independents may accept shelf-stocking services from suppliers, services that the major chains are prohibited from accepting.

Existing provincial legislation also provides the smaller retailer with advantages over the larger retailer. Pursuant to the Assessment Act,* retailers owning five stores or less are subject to tax equal to 30% of assessed value; chains of more than five stores must pay 50%. Pursuant to the Retail Business Holidays Act,† retailers whose selling and display space is less than 2,700 square feet and who employ less than three persons, are able to open on holidays including Sundays; their larger competitors are not.

The Commission has discovered the innovation of the minor chains and independents to be quite remarkable. The Knob Hill Farms chain has proved to be a veritable thorn in the side of the major retail chains in Toronto by introducing the "food-terminal" concept. Food terminals are stores ranging up to 160,000 square feet in size with a country-market-type atmosphere combining warehousing with retailing functions to avoid storage and distribution costs. The two D'Arrigo chains in Toronto, D'Arrigo's Supermarkets and D'Arrigo Food Markets, earn their share of the metropolitan market by catering to an Italian and Greek clientele which prefers plentiful fresh fruit and vegetables of good quality, and fresh meat which is sliced into retail cuts on the premises and not wrapped until time of sale. Both chains have grown in store numbers and presumably in sales since their beginnings in the early 1970's. Such success stories are not limited to Toronto. The Calbeck chain in

* R.S.O. 1970, s. 71(e) and (j).
† R.S.O. 1975, 2nd Sessions, s. 1-3 (a)-(c).

the Brantford area attributes its expansion to giving better service than the chains and to developing a local consumer franchise by supporting community teams and civic events.

Having described the Ontario retail food market structure, I now turn to market performance as measured by profit rates and other efficiency indicators.

The Commission's consultants submitted evidence that, for the last three fiscal years, there is no significant difference between the major chains and minor chains surveyed in the area of profits. This finding applies to gross margins, net margins after tax and returns on equity after tax. This evidence is presented in tabular form in Table 13-K. Furthermore, the returns on capital and equity of the major food chains do not appear to be out of line with returns on capital and equity in other merchandising companies. This comparability is indicated in Table 13-L.

One available measure of efficiency in market performance is the amount of sales per square foot that a food retailer transacts. According to Mr. Tigert, who uses this statistic to analyze investment opportunities, sales per square foot is the best available measure of efficiency. His estimations show that Canadian supermarket chains achieve superior sales per square foot compared to their counterparts in the United States. This data is represented in Table 13-M.

TABLE 13-K

SUMMARY OF RETAILER FINANCIAL STATISTICS

	Small Chains	Large Chains	Average	Significant Difference 95% Confidence Level
A. Latest Period				
Gross Margin	21.1%	20.0%	20.9%	no
Net Margin (after tax)	0.9%	1.1%	1.0%	no
Return on Equity (after tax)	18.3%	16.1%	17.1%	no
B. Latest 3 Period Average				
Gross Margin	20.3%	19.3%	20.1%	no
Net Margin (after tax)	1.0%	1.0%	1.0%	no
Return on Equity (after tax)	14.7%	14.3%	14.5%	no

Anti-Inflation Board Survey of Retailers

	Net Margin (after 50% tax)	Return on Equity (after 50% tax)
1975	1.10%	12.20%
1976	0.70%	9.15%
1977	0.85%	10.45%

NOTE: These figures include all off-invoice allowances.

SOURCE: Retailer questionnaire and A Study of Profit Margins in the Food Industry, Anti-Inflation Board (Ottawa: 1978).

TABLE 13-L

COMPARISON OF OPERATING RESULTS OF FOOD AND NON-FOOD MERCHANDISING COMPANIES IN CANADA IN 1978

Company	Sales	Return on Food Merchandising Companies in Canada		Return on Non-Food Merchandising Companies in Canada	
	$ millions	Capital %	Equity %	Capital %	Equity %
Loblaw Companies					
Canada	2,645				
U.S.A.	1,602				
	4,247	15.0	11.0		
Dominion Stores					
	2,405	20.2	15.9		
Provigo Inc.					
Food-Canada	1,477				
Drugs-Canada	160				
Food-USA	400				
	2,037	23.9	20.6		
Canada Safeway					
Canada	1,880				
Germany	105				
	1,985	22.3	13.6		
Steinberg Inc.					
Supermarkets	1,620				
Other Division	297				
	1,917	15.3	13.6		
Oshawa Group					
Food Distrib.	1,053				
Other Division	284				
	1,337	11.7	8.6		
A&P (Canada)	431	8.1	5.5		
Sobey's Stores	309	15.4	13.0		

TABLE 13-L

COMPARISON OF OPERATING RESULTS OF FOOD AND NON-FOOD MERCHANDISING COMPANIES IN CANADA IN 1978
(continued)

Company	Sales	Return on Food Merchandising Companies in Canada		Return on Non-Food Merchandising Companies in Canada	
	$ millions	Capital %	Equity %	Capital %	Equity %
Simpson-Sears				14.4	14.1
Hudson's Bay				11.4	13.2
Woolworth F.W.				19.1	12.4
Canadian Tire				16.6	12.1
Woodwards				15.1	12.7
Simpsons				10.2	9.1
Zeller's				20.5	19.6
K-mart Canada				20.0	12.8
Consumers Distributing				38.0	28.2
Dylex				28.9	20.1
Grafton Group				40.2	29.0
Revelstoke				16.6	15.7
Reitman's				38.4	22.6
AVERAGE:		17.6	12.7	15.7	14.4

NOTE: Returns on capital and equity for several food merchandisers are calculated on both food and non-food operations because returns are calculated over the company's entire equity base. In all cases the large majority of sales accrue from Canadian food merchandising, as the sales figures indicate.

SOURCE: J. Donald Tigert, Burns Fry Limited

TABLE 13-M

SUPERMARKET CHAINS' SALES PER SQUARE FOOT

Calendar Year 1977

Canada	Sales per square foot
Dominion	$301
Steinbergs	252
Canada Safeway	244
Loblaw (Ontario)	240
A&P	198
Woodward's	300
Food City	185
Provigan/AVA	252
Sobey's	188
Zehr	211
AVERAGE	$251

United States	Sales per square foot
Safeway	$200
A&P	189
Kroger	221
Winn-Dixie	186
American Stores	214
Lucky Stores	230
Jewel Cos.	234
Food Fair	181
Albertson's	223
Grand Union	156
Pathmark	383
Fisher Foods	250
Publix (est.)	250
Dillon Cos.	262
Stop and Shop	259
AVERAGE	$211

SOURCE: Estimates by J. Donald Tigert, Burns Fry Limited.

On this measure of efficiency, independents may do equally well, if not better. Seventy-one independent stores surveyed by Canadian Grocer in the December, 1978, edition, reported average sales per square foot of $345.00 which is better than the average figure reported for the ten major Canadian chains. This comparison should be treated with caution since the data were generated from two separate surveys, the technical details of which were not reported with the results.

I now examine the effect of discounting on retail concentration. Data collected by the Commission's consultants on this issue are reproduced as Tables 13-N, and 13-O. From these tables, one can see that there is a significant difference in the level of rebates received by small chains -- including what I have referred to as "minor combination chains" -- and large chains on such products as beverages, canned fruit and vegetables, cereal and frozen foods. On the other hand, there is no significant difference on such products as baked goods, dairy products, fresh produce, meat and soup. Most importantly, when all products are weighted according to their importance in terms of sales, there is no significant difference in rebates received. Weights used are shown in Table 13-P.

That there is no significant difference is a logical result when it is considered that the small chains and the vast majority of independents buy many of their products through wholesalers and through buying groups. This tends to equalize the buying advantage that the major chains in Ontario would otherwise have in respect of their market

TABLE 13-N

SUMMARY OF REBATES RECEIVED BY RETAILERS

(% of retailer purchases)

Food Product	Small Chains	Large Chains	Average	Significant Difference 95% Confidence Level
Baked Goods	6.1%	9.4%	7.6%	NO
Beverages	1.3%	5.3%	3.0%	YES
Canned Fruit	1.4%	8.4%	4.7%	YES
Canned Vegetables	1.0%	9.1%	5.0%	YES
Cereal	1.3%	5.0%	2.9%	YES
Dairy Products	17.5%	25.0%	20.8%	NO
Fresh Produce	0.4%	2.4%	1.4%	NO
Frozen Food	0.6%	3.8%	2.1%	YES
Meat	1.8%	3.5%	2.5%	NO
Soup	1.9%	4.1%	2.9%	NO
Simple Average	3.2%	7.5%	5.1%	YES
Weighted Average (see Table 13-O)	7.4%	7.7%	7.5%	NO

NOTE: These figures include all off-invoice allowances.

SOURCE: Retailer questionnaire.

TABLE 13-O

ANALYSIS OF REBATES RECEIVED BY RETAILERS

Food Product	Major Combination Chains	Minor Combination Chains	Major and Minor Grocery Convenience Chains	Unaffiliated Combination Independents	Franchised and Voluntary Group Combination Independents	Average	Significant Difference 95% Confidence
Baked Goods	9.4%	2.4%	8.0%	8.6%	11.6%	8.3%	NO
Beverages	5.3%	0.5%	1.7%	8.1%	5.1%	4.6%	YES
Canned Fruit	8.4%	2.2%	0.9%	11.2%	10.2%	7.2%	YES
Canned Vegetables	9.1%	1.1%	0.9%	11.7%	8.6%	7.4%	YES
Cereal	5.0%	1.9%	0.9%	8.5%	4.9%	4.8%	YES
Dairy Products	25.0%	26.1%	13.3%	18.6%	27.4%	21.0%	YES
Fresh Produce	2.4%	0.0%	0.7%	0.5%	4.5%	1.5%	YES
Frozen Food	3.8%	1.3%	0.9%	5.3%	2.9%	3.1%	YES
Meat	3.5%	0.6%	2.4%	6.4%	5.8%	4.0%	NO
Soup	4.1%	3.5%	0.9%	4.6%	3.1%	3.4%	NO
Weighted Average	7.7%	4.6%	6.3%	8.2%	9.1%	7.3%	NO

NOTE: The following groups have a combination store sales mix - Large Chains, Small Combination Chains, Small Independents, Small Sponsored - and are weighted accordingly. The Convenience Stores group have a grocery store sales mix, and are weighted accordingly.

SOURCE: Retailer questionnaire.

TABLE 13-P

RELATIVE IMPORTANCE OF SALES BY RETAILERS

Food Product	Grocery Stores		Combination Stores	
	Sale %	Relative Weight	Sale %	Relative Weight
Baked Goods	6.3%	11.8%	3.9%	5.4%
Beverages	11.1%	20.7%	2.8%	3.9%
Canned Fruit	2.2%	4.1%	5.3%	7.4%
Canned Vegetables	2.2%	4.1%	5.3%	7.4%
Cereal	1.3%	2.4%	1.4%	2.0%
Dairy Products	18.6%	34.8%	10.3%	14.4%
Fresh Produce	1.7%	3.2%	8.5%	11.9%
Frozen Food	5.4%	10.1%	6.6%	9.2%
Meat	2.5%	4.7%	22.3%	31.0%
Soup	2.2%	4.1%	5.3%	7.4%
TOTAL	53.5%	100.0%	71.7%	100.0%

NOTE: 1. Statistics Canada figures for canned goods are reported in aggregate only (6.5% for grocery stores, 15.8% for combination stores). We assume that canned fruit, canned vegetables and soups each accounted for one third of the canned foods sales. Data for the small chains and independents are from the grocery stores columns, and for the large retailer are from the combination stores columns. The data are for Ontario.

SOURCE: Statistics Canada, Retail Commodity Survey, 1974 (catalogue 63-526).

power due to superior buying volume and important market share. From this evidence, the Commission concludes that the level of rebates received is not a deteriminant of concentration as between the group of major chains and the group of minor chains and independents.

In summary, it seems safe to say that minor chains and independents have lost a significant percentage of retail food market share to the major chains, both in Ontario and nation-wide. Unsegregated data make it impossible to identify which categories of minor chains and independents have lost or gained over the last forty-five years. It seems equally safe to say that this trend has abated in recent years and that there are reasons to believe that minor chains and independents will continue to hold a substantial share of the market. In any event, discounting is not one of the determinants of concentration at the retail level.

CONCLUSIONS

The following is a summary of my conclusions on the evidence examined in this chapter.

1. Concentration at the producer level ranges from atomistic (many sellers - many buyers) to monopolistic. Increasing values of farm products are subject to marketing boards, a unique type of monopoly sanctioned by the Legislature. The average farm size is increasing and barriers to entry in the form of capital investment requirements are higher than before. Therefore, I conclude that

concentration at this level of the food chain appears to be increasing.

2. Concentration at the processor level is high and moderately high for many commodities. However, I conclude that discounting is not a cause of high degrees of concentration at the processor level because there is no correlation between the rebate levels and the size of processors nor between rebate levels and financial performance of processors.

3. Concentration at the wholesaler level is moderately high and is characterized by an oligopoly of three corporations. However, I conclude that discounting is not a cause of the degree of concentration at the wholesaler level because there is no correlation between the rebate levels and the size of wholesalers. Furthermore, the degree of concentration in the wholesale market is not allowing the firms to earn higher than normal profits.

4. Concentration at the retailer level is moderately high. The degree of concentration has increased during the last ten years but there is significantly less of an increase during the last five years. I expect that future increases, if any, will likely be minimal due to the strength of various competitors in the Ontario retail food market. I conclude that discounting is not a

cause of increasing concentration at this level because there is no correlation between the rebate levels and the size of retailers nor between rebate levels and financial performance of retailers.

CHAPTER 14

LOSS-LEADER SELLING

GENERAL

The Commission's terms of reference direct it to inquire into "discounts, allowances, rebates or other forms of payment...paid or allowed directly or indirectly to purchasers thereof other than...directly to the consumer" (underlining mine).

Loss-leader selling refers to the marketing of food or grocery food products by retailers directly to the consumer and thus may appear to be expressly outside the terms of reference. However, certain allegations were made during the Inquiry to the effect that loss-leader selling by retailers to consumers resulted in severe pressure as between retailers and suppliers, the type of pressure the Commission considered relevant to its investigation of food marketing practices in Ontario. Loss-leader selling will also be discussed in Chapter 17, Rebates and the Law.

WHAT IS A LOSS LEADER?

A loss leader may be defined as being a product offered for sale at less than cost.

This definition is too simplistic. The witnesses at the Inquiry had various definitions, but none were totally acceptable. The problem of definition is one of

determining a suitable cost to use as the level below which loss-leader selling occurs.

Two definitions of cost are superior to others:

(a) The first definition describes the retailer's cost as the "net acquisition cost" of the product.

For example, assume the retailer purchased the product from a supplier for $1.00 per unit less 15¢ per unit discount; the "net acquistion cost" would be 85¢ per unit. Any price to the consumer lower than 85¢ per unit would be a loss leader.

(b) The second definition describes the retailer's cost as the "shelf cost" of the product. Shelf cost includes the retailer's net acquisition cost of the product <u>plus</u> the expenses required by the retailer to actually sell the product.

For example, assume the net acquisition cost of a unit is 85¢ as above. Assume further that the retailer incurs expenses in the amount of 3¢ per unit to deliver the product to the store via a warehouse plus 15¢ to pay labour for installing the product on the shelf and for store maintenance and other overhead. The shelf cost would be $1.03 per unit and any price to the consumer lower than $1.03 would be a loss leader.

As a matter of interest, a document published by the Department of Justice in 1954 in connection with an Inquiry by the Restrictive Trade Practices Commission contained seven definitions of loss-leader selling.*

PRODUCTS SUBJECT TO LOSS-LEADER SELLING

Many products were mentioned by witnesses as being subject to loss-leader selling although it was not always clear to what definition the witness was referring. The evidence indicated that loss-leader selling occurred mainly in the staple foods; in fact, one retailer testified that he sold all staple foods at a loss.

The consumer is very price sensitive as to staple foods because of the regularity with which they are purchased. Retailers are aware that they will attract consumers to their store if they reduce the price of the staples below competitors' prices.

The following is a list of products which are most frequently sold as loss leaders, according to testimony: bread, milk, eggs, meat, sugar, potatoes, butter, margarine, apples, onions, carrots and peaches. The most frequently mentioned products are at the beginning of the list.

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* Restrictive Trade Practices Commission, Loss-Leader Selling, (Department of Justice, Ottawa: 1954) pp. 5-12.

This list is not definitive. Any food product purchased frequently by consumers is susceptible to loss-leader selling.

EVIDENCE CRITICAL OF LOSS-LEADER SELLING

Loss-leader selling was alleged by various witnesses to have a detrimental effect on the food industry both in the short run and the long run.

Three organizations -- The Bakery Council of Canada, The Ontario Fresh Potato Growers' Marketing Board, and The Independent Milk Distributors Association -- were particularly critical. I shall deal with each of these organizations' complaints later.

Following is a summary of the alleged detrimental effects of loss-leader selling:

1. In the short run:

    (a) Suppliers are pressured into reducing their price so that retailers minimize the loss incurred in selling below cost.

    (b) Suppliers' normal sales and shipment patterns are upset.

    (c) Suppliers of name brand products may have to compete with house brand products sold at loss-leader prices.

(d) Retailers compete with a retailer who has initiated a loss leader by offering their own loss leader. This multiplies the pressure on the supplier to sell at a reduced price.

(e) Retailers who cannot afford to loss leader lose customers. This is alleged to be particularly harmful if the retailer is selling a limited line of products or relying heavily on one product, such as milk.

(f) Retailers who cannot match the loss leaders may be unable to sell their usual quantities. Such merchandise ultimately goes stale and is wasted.

(g) Consumers are deceived: they believe they are getting a bargain on one item while, in fact, they may be paying more for other items.

(h) Consumers engage in inefficient use of resources to take advantage of loss-leader selling. For example, they freeze bread unnecessarily or they drive long distances for a bargain.

2. In the long run:

(a) Consumers develop a false sense of the product's value because the prices are not related to production costs.

(b) Suppliers whose products decrease in price to accommodate loss-leader selling, and suppliers and retailers who must compete with loss leaders, experience deteriorating financial positions. When this occurs, the firms and employees that depend on these suppliers and retailers lose income and employment.

(c) As a result of (b), a monopolistic situation may develop. If so, consumers could be faced with higher prices and less services while farmers may be obliged to accept lower prices.

EVIDENCE SUPPORTIVE OF LOSS-LEADER SELLING

The large retailers testifying before the Commission admitted to using loss-leader selling as a "minor marketing tool" or as a "competitive response" to loss-leader selling by other retailers. They and other witnesses supported its use for the following reasons:

(a) Suppliers are not pressured into reducing their prices to accommodate a loss-leader sale any more than they are usually pressured to sell at the lowest possible price.

(b) Suppliers of certain fruits and vegetables are protected by marketing boards from any pressures that occur as an incident of loss-leader selling.

(c) Loss-leader selling increases sales of the products sold at loss-leader prices. In fact, loss-leader selling may prevent unsold merchandise from going stale.

(d) New suppliers and new retailers use loss-leader selling and advertising as a means of gaining entry into the market. If they are successful, their entry enhances and promotes competition in these markets.

(e) Retailers do not necessarily mark up other items to compensate for the loss on the loss-leader sale. The loss is underwritten by the company in the hope of attracting new customers. Alternatively, the loss is compensated by the purchase of other items in a greater volume than before.

Item (e) requires an example in explanation. Assume five new customers buy a loss-leader item on which the retailer takes a loss of 5¢ per item. The retailer's loss would appear to be 25¢. However, if three of the five customers buy an additional item on which the retailer makes a profit of 10¢, then the retailer has made a profit of 5¢ by loss-leader selling although no item was marked up higher than normally. Furthermore, even if none of the new customers buys an item other than the loss leader, the retailer may eventually earn a profit if the new customers decide in the future to do their regular shopping in that store.

(f) Retailers are able to reduce their own inventories and the over-supply of food products, especially farm products, by loss-leader selling.

LOSS LEADERS AND THE CONSUMER

The average Ontario consumer has developed quite sophisticated shopping skills. Consumers are able to reduce their grocery bills by purchasing loss leaders; this is particularly beneficial as most loss leaders are staple food products. Also, consumers with large families may buy a loss leader, for example soft drinks, in large quantities and store it.

Consumers further reduce their grocery bills by "shopping the specials." They will shop at various retail outlets that are featuring "specials," low-priced products which may or may not be loss leaders.

Mrs. Ruth Jackson of the Consumers' Association of Canada testified that consumers with sufficient money, time, transportation, storage facilities and large families benefit more than other consumers from specials. Consumers such as the elderly, who do not usually buy in quantity, and the poor, who do not have storage or transportation, do not benefit as much from specials.

FOOD PRODUCTS PARTICULARLY AFFECTED BY LOSS-LEADER SELLING

The benefits and detriments of loss-leader selling are illustrated vividly in the evidence relating to the bakery

industry, the milk home-distribution industry and the potato industry.

1. THE BAKERY INDUSTRY

The Bakery Council of Canada, in conjunction with the Canadian Council of Teamsters and the Retail Merchants Association of Canada, presented a brief to the Commission. The brief noted particularly the decline in the number of bakeries and bakery employees in Ontario from 1965 to 1976 which is represented in the form of a chart as follows:

	1965	1976
Number of bakeries in Ontario	766	456
Number of employees	12,600	9,924
Average number of employees per bakery	16.5	21.8

The Council submitted that loss-leader selling contributed to this decline. The brief of the Council concludes: "Loss leader pricing policies by large and small retail chains are one of the contributing factors forcing independent bakeries and grocers out of business."

The brief recommended that the Ontario Legislature should enact legislation restricting loss-leader advertising of breads to point-of-sale advertising. It is the submission of the Council that retailers would not sell bread at loss-leader prices if they could not advertise

these prices elsewhere than on the shelves or at the check-out counter. The Council specifically rejected the solution adopted in the province of Quebec which, in addition to restricting price advertising to the point of sale, sets a minimum price for bread.

The Commission heard evidence from Mr. Jack Levine, President of Steinberg Inc., that the Quebec solution has contributed to the decline in over-all bread consumption and has therefore contributed to the decline in the numbers of bakeries, especially small bakeries, in that province.

Representatives of the Council admitted, under examination, that factors other than loss-leader selling have contributed to the decline of the bakery industry in Ontario. These other factors are:

(i) increasing affluence of consumers;

(ii) increasing sale of substitutes for bread, for example, pizza;

(iii) difficulty in finding qualified tradesmen;

(iv) high wage levels;

(v) rising cost of ingredients; and,

(vi) rising cost of machinery.

I am unable to endorse the Bakery Council's recommendations for the following reasons. In my opinion, the Bakery Council's proposals would probably have adverse effects on the bread industry in Ontario. The Quebec experience with the prohibition of price advertising in regard to bread does not indicate that such legislation is

capable of halting the decline in numbers of bakeries or the loss of jobs in the industry. Structural factors and economies of scale probably account for the survival of larger bakeries rather than smaller bakeries.

Therefore, enacting the Bakery Council's recommendation would have limited effect on the changes that are presently occurring in Ontario's baking industry while it may adversely affect the price of bread available to the consumer. This is because it is unlikely that retailers would reduce prices if they are unable to advertise the reduction.

2. MILK HOME-DISTRIBUTION INDUSTRY

The Independent Milk Distributors Association submitted a brief to the Inquiry. The Association consists of nine member firms which sell milk on a door-to-door basis and also wholesale it to small stores and specialty shops.

The general argument put forward by the Association was that loss-leader selling, by the large retail chains in particular, is shifting milk buying away from both small retail and door-to-door customers of the Association members. The Association's members cannot offer milk at loss-leader prices because the members have no other products with which to recoup their losses.

The Association was concerned with the level of rebates that the larger retail chains are receiving on milk purchases. It also questioned whether these retailers are

getting larger rebates when they institute loss-leader selling.

The evidence received by the Commission -- including testimony of dairy processors and retailers, and confidential material received from retailers and processors -- answers these questions in the following manner:

(i) rebates to large chain retailers average 25% to 30% of purchases of milk. This level can be approximated by large independent retailers, especially those that are part of a buying group; and,

(ii) rebate levels in milk do not vary with the retail selling price but only with the volume purchased by retailers from processors. (See Chapter 6 on milk rebates for amplification of this subject.)

The solutions recommended by the Association include first, a prohibition of loss-leader selling and price advertising of loss-leader products; and second, establishment of minimum prices at the processor and retail levels. Minimum price legislation was considered in the Report of the Inquiry on Wholesale and Retail Pricing Practices conducted by the Milk Commission of Ontario a few years ago. The Commission rejected this solution.

In my opinion, both of the Association's recommendations may hamper the aggressive marketing of milk to consumers, in which case the price of this staple commodity would almost certainly rise. If the price of any commodity

increases, economic theory suggests that consumption will decrease depending on the elasticity of the commodity's demand.

I can see that controlled milk prices at all levels would, to some extent, protect the home-delivery business since such controls would probably narrow the difference in prices between store-bought milk and home-delivered milk. However, I am not convinced that protection of the home-delivery business would be to the benefit of the majority of milk consumers in Ontario who would face price increases for the reason cited above.

Unfortunately for the Association member, the fact is that door-to-door distribution of milk is a business which has undergone considerable change due to structural factors and changing patterns of buying by consumers. The structural changes are that the costs of transportation, including fuel, have escalated far more rapidly than most other costs putting transport-related industries at a severe price disadvantage. As a result, consumers are today more likely to buy milk at a corner convenience store or during their weekly supermarket shopping.

(c) The Potato Industry

Mr. Les Armstrong, secretary-manager of the Ontario Fresh Potato Growers' Marketing Board, testified at the Inquiry.

Mr. Armstrong's testimony is directed at the alleged market disruption caused by loss-leader selling of large retail chain stores. The witness indicated that negotiations become more intense when a retailer intends to start a loss-leader promotion. The results of increased negotiation pressure, he contended, are usually lower prices to the producer.

Mr. Armstrong did not blame the retailers or packers but the Ontario producers themselves for their inability to present a common front in marketing their product. Producers, he testified, have received prices that are lower than normal during the past three years mainly because of oversupply and the inferior marketing image of Ontario potatoes.

Again, it is my conclusion that loss-leader selling is not the major cause of the producers' problems. These problems are mainly due to an imbalance of supply and demand and to a deficiency of information flows to the producer: the producer is often unaware of alternative buyers in the marketplace. From Mr. Armstrong's evidence, it would appear that steps are being taken to correct these basic problems.

CONCLUSIONS

The following are my conclusions on the evidence examined in this Chapter:

1. There is no common definition of "loss leader"; the definition which I have chosen to use is: the reduction of price below the retailer's shelf cost which includes the retailer's net acquisition cost and all costs incurred up to the point where the food is sold to the consumer.

2. Staple food products are, from time to time, subject to loss-leader selling by major retailers. Such selling may stimulate increased pressure upon suppliers for reduced prices. Such selling certainly reduces the price of the product to the consumer and increases the sales of the farm products involved, at least in the short run. There is no evidence that retailers uniformly mark up prices on other products to compensate for losses incurred during the loss-leader sale.

3. Associations representing suppliers in three industries -- bakeries, milk distributors, and potato growers -- alleged that loss-leader selling has had a detrimental effect financially on their members. However, these industries have all undergone structural or market changes or deficiencies that may cause all or part of their distress. Therefore, I cannot conclude that the elimination

of loss-leader selling would outweigh the present benefits of such selling to the consumer and to the farmer.

CHAPTER 15

LISTING AND DELISTING

GENERAL

Throughout the Inquiry, several witnesses expressed critical views about the listing allowances that had to be paid by a manufacturer to get his products on the large retailer's shelf. In addition, allegations were made that certain manufacturers were delisted for failure to pay sufficient rebates.

BACKGROUND

The listing allowance has been described in Chapter 3; to reiterate, the allowance is paid in return for services provided by the retailer -- including administrative services and often, various promotional activities -- upon the introduction of a manufacturer's new product. Though the extent of services provided may vary, it must be recognized that certain basic economic facts underlie the listing of products for sale on the retailers' and wholesalers' shelves.

A food manufacturer, when he introduces a new product for sale, realizes that he must get it on to a large retailer's shelf in order to sell it in volume sufficient to realize a profit on his investment. A large manufacturer may conduct an extensive mass media campaign -- television, radio, newspaper -- so as to create a consumer demand for the product. If the demand is created, retailers are

anxious to stock his product. It is good economics for a retailer to have on his shelf a product that will "move" (meaning, sell in volume).

A small manufacturer likely cannot afford a national advertising campaign. As an alternative way of marketing, the small manufacturer may offer a listing allowance, sometimes called "introductory allowance," to the retailer to sell his product. Even the large manufacturer may offer a listing allowance to supplement his advertising campaign. The survey performed by the Commission's consultants indicated that 5.9% of food suppliers offered introductory allowances to retailers on name brand products over a one-year period. The average size of this allowance is 1.8% of annual sales of all products. (See Tables 2-A and 2-B in Chapter 2.)

The retailer also has to face certain economic facts. His shelf space is valuable and limited. A new product must pay its way. In order to shelve a new product, the retailer must usually remove an item which, presumably, has significant sales movement. In addition, the retailer incurs expenses in connection with introducing a new product. These costs include: product evaluation, warehouse alterations, product promotion and shelf-space alterations. What products to list or delist is a day-to-day decision calculated by the management of both retailers and wholesalers. They endeavour not to buy an "Edsel."

EVIDENCE CRITICAL OF LISTING ALLOWANCES

(a) The Ontario Federation of Agriculture acknowledged that a listing allowance may properly relate to the expenses and risks associated with the introduction of a new product. The O.F.A. questioned, however, the allocation of these risks and expenses to the supply sector as opposed to the retail sector. The Federation also pointed out that suppliers may have to increase the list price in order to accommodate these allowances; such increases make it more difficult for the small retailer to stock the new product, it is alleged.

(b) The Grocery Products Manufacturers of Canada alleged that listing allowances increase substantially the cost of introducing a new product. The G.P.M.C. also claimed that such allowances effectively represent a charge for nothing more than the availability of retail shelf space.

The G.P.M.C. further submitted that the public is being deprived of valuable new products because of the high cost of "listing allowances," a cost disproportionate to the risks involved. The current trend towards higher charges places the retailer rather than the consumer as the final arbiter of what products will appear on the shelves, the G.P.M.C. alleged.

As a general solution to discounting problems, express buyer liability under the existing federal law is recommended by the G.P.M.C. I shall consider the issue of buyer

liability in Chapter 16, Rebates and the Law. It is worthy of note that the G.P.M.C. does not recommend specific legislation to deal with the problem of listing allowances. Instead, the Association prefers to let the natural workings of the market place counteract any abuse of otherwise appropriate practices.

(c) Mr. Arthur Ruttan, President of Ruttan Diet Foods, testified at the Inquiry. The firm specializes in the manufacture and distribution of diet food products.

In 1978, his firm developed a new artificial sweetener that it endeavoured to sell in the food stores, Mr. Ruttan stated. Loblaws and Dominion Stores asked for a $5,000 listing fee to list the product. Mr. Ruttan's firm was unable to pay this amount in cash and instead offered a reduction of 10% per case provided the chain ordered at least $5,000 worth of product. In Mr. Ruttan's words, this gave the chain an incentive to "push the product." Loblaws purchased product from Ruttan Diet Foods on this basis. Upon cross-examination by counsel for Loblaws, Mr. Ruttan admitted that Loblaws received a total of only $500 in discounts on $5,000 of purchases.

Upon cross-examination by counsel for Dominion Stores, Mr. Ruttan further admitted that it was necessary to promote his product in order to overcome the "saccharin scare," referring to widely publicized scientific research linking artificial sweeteners with cancer in laboratory animals. He admitted that the 10% allowance paid to Dominion helped to promote his product.

(d) Mr. Vincent de Souza is an importer and exporter of food products. In 1971, he and his partner were importing into Canada a long grain rice product. This type of rice is sold in five pound bags, mainly to customers of ethnic background. It is apparently a good quality rice. Mr. de Souza negotiated with the buyers of Food City, Loblaws, Dominion Stores and Knob Hill who were interested in the purchase of his rice.

The witness was able to negotiate a sale of 7,000 bales to Food City after agreeing to discounts totalling 50% of the purchase price. However, Food City did not place further orders after the initial purchase, he testified, because his firm fell into financial difficulties.

Mr. de Souza offered Dominion Stores a 22% discount based on a suggested retail price of 24 1/2¢ per pound. His competitors' retail price was approximately 40¢ per pound. According to Mr. de Souza, the buyer indicated it would be difficult to get the purchasing committee to buy unless a listing allowance was also offered. The buyer suggested the allowances should have a value of $10,000, to be calculated as a percentage discount on orders. Mr. de Souza testified that to grant this additional discount, based on a 24 1/2¢ selling price, would have meant a loss to him.

Mr. de Souza then made another offer to Dominion Stores: he suggested a retail selling price of 33¢ per pound and agreed to discounts of approximately 50%. The parties did not reach agreement. Dominion Stores

eventually advised him that they had decided against buying another line of rice.

Similar presentations were made by Mr. de Souza to Loblaws and Knob Hill Farms, without success.

EVIDENCE SUPPORTIVE OF LISTING ALLOWANCES

(a) The Retail Council of Canada submitted that introductory allowances cover the lost opportunity return for the items replaced and the risk factor where new product failure rate is high. The allowance is intended as well to offset some of the administrative expenses associated with the product change: store notification, accounting and computer recording.

The Retail Council is of the view that the cost of new product introduction should be attributed as much as possible to the manufacturer or supplier of the product rather than to the retailer who must spread the cost of a new item across all items carried with resulting higher prices to the consumer.

(b) Mr. David A. Nichol, President of Loblaws Limited, provided the Commission with some concrete evidence on this issue. Mr. Nichol referred to research performed by the A.C. Neilson Company. The research indicates that listing a new product is a very expensive procedure for a supermarket, involving costs of evaluation, warehousing, resetting shelf space (in Loblaw's case, of 132 stores), and promotion. Mr. Nichol testified that Loblaws has

established a company policy that for every product listed, another must be delisted; therefore, costs of delisting items and disposing of excess stocks of the items delisted must be considered. New products not only are costly and disruptive for a supermarket to handle but they are also risky: 53% of new products fail.

Mr. Nichol testified that Loblaws receives an introductory case allowance which helps to defray the costs mentioned above. He further suggested that such allowances are received by every food distributor in Ontario. He also testified that Loblaws' co-operative program distributed to suppliers suggests a $2,500 listing allowance. This fee would ensure that all 132 Loblaws stores stock and order the new item but, so far, no supplier has purchased this program.

(c) Mr. Allen Jackson, President of Dominion Stores, testified that the name "listing allowance" was originated by wholesalers who charged suppliers a listing fee to be entered in wholesale catalogues. Dominion Stores, he testified, has never received a listing fee as explained below.

According to Mr. Jackson's evidence, a supplier makes an introductory offer. This offer may take a variety of forms. Some examples are one free case if ten are purchased, or two dollars off per case, or an allocation of promotional dollars to buy promotions.

The witness stated that whatever form the introductory allowance takes, Dominion Stores must earn the allowance and does so by promoting the product. He was emphatic that suppliers who call these allowances listing fees are incorrect: "It's not a listing fee. It's a sum of money that is used to promote the product. We have to earn it."

He submitted that in addition to bearing the costs of stocking a new product, the retailer bears the brunt of the loss when a new product fails. A new product is not bought on a guaranteed sales basis, he stated; therefore, if the product does not sell, the retailer must reduce its price and perhaps incur a loss in the process. He added that, regardless of the promotional allowances or other rebates offered on a new product, the product is of no value unless it will sell.

(d) The President of Steinberg's, Mr. Jack Levine, testified that his firm receives listing allowances but only insists on them if other retailers are receiving them. Mr. Levine agreed with the G.P.M.C. that listing allowances may discourage the presentation of new products but he disagreed that allowances paid are disproportionate to listing costs.

DELISTING PRODUCTS

General

Allegations were made at the Inquiry that certain large retail chains delisted products because the supplier

would not provide higher rebates. These allegations are serious because, as indicated in the previous sections, it is vital for a manufacturer to get his product on the shelves of the major chain stores.

It will be seen, however, that the evidence pertaining to this allegation is quite contradictory.

EVIDENCE CRITICAL OF DELISTING

(a) The Grocery Products Manufacturers of Canada made several references to the delisting of products in its presentation. I quote from the Association's brief:

> "...[A] number of manufacturers perceive that a wrong response to a retailer's request for promotional monies will lead to disproportionate consequences which affect the whole business of a manufacturer with that particular retailer, (e.g., a situation in which a retailer indicates that a failure to provide the requested allowances could result in a product delisting)... The reality today is that purchases by any one of the big retailers tend to be large enough in relation to the production volumes of most products that loss of any one of these purchases can have a significant effect on unit costs and volumes, and thus on profits, of affected manufacturers."

Mr. David Morley is President of the G.P.M.C. He indicated that in January, 1979, the firm of Coopers &

Lybrand, on behalf of the G.P.M.C., asked 93 members of the Association whether they had been delisted as a consequence of refusing to pay a particular rebate. Of the 93 surveyed, 50 replied. Of these responses, 31 companies indicated they had in fact been delisted while nineteen said they had not. Mr. Morley, in cross-examination, stated that the members surveyed were not asked whether the delisted product was selling in enough volume to justify continuance.

(b) The Ontario Federation of Agriculture stated that established dairy products are delisted at the whim of a chain for such reasons as untimely delivery. The O.F.A. alleged that this delisting then gives the chain an excuse to impose listing fees as a condition of resuming purchases. These allegations were not substantiated by evidence to this effect.

(c) Mr. Jack Morgan is a food broker, engaged for several years in the business of exporting and importing food and food products. Mr. Morgan testified that it is common practice for a retailer to delist a product if the supplier does not meet a trade demand. He considered it as a normal part of the food business operation.

In Mr. Morgan's view, there is no difference between paying a lump sum listing fee or allowing rebates on the initial price. All the supplier and retailer are really concerned with is the net price or "bottom line." He testified that those persons who criticize listing fees do so out of ignorance as to how business operates.

Mr. Morgan also gave testimony as to an incident involving the alleged delisting of a major food manufacturer. According to Mr. Morgan, Kellogg-Salada Canada Limited "reduced their rebate program" and, as a consequence, was delisted by Dominion Stores.

As this incident was the only direct evidence of delisting due to discounting practices, I instructed counsel to thoroughly investigate the allegation. The Executive Vice-President of Operations for Kellogg's denied any knowledge of the situation. Neither Commission Counsel, Mr. Hull, nor myself, was satisfied with this answer. Further examination disclosed the names of senior officers in the company at the time of the alleged delisting.

Subsequently, evidence from these officers was obtained in the form of telexes filed as exhibits. Mr. Gerry Robinson, President of the company at the time of the incident (1962) and presently Managing Director of European operations, responded that he does not recall any instance of mass delisting although he does recall that the company changed its merchandising plan during the year in question so as to conform with the <u>Combines Investigation Act</u>. Mr. William Nicolson, National Sales Manager at the time and presently Managing Director of Australia-Middle East Operations, responded that Kellogg's 1962 merchandising plan was discontinued because of the company's fear that it was in contravention of the Combines Act and because the plan's costs were greater than anticipated. As a consequence of changing the plan, Kellogg "lost distribution of some sizes and products in a number of outlets - this was so with

Dominion Stores..." to their competitors but recouped this loss when the plan was changed in 1963.

Representatives of Dominion Stores also gave evidence as to the Kellogg incident. Mr. Allen Jackson, President of Dominion Stores, testified that Kellogg's discontinued a rebate on sales to Dominion Stores in the amount of 1 1/2% to 2%. The cost of Kellogg's products was not reduced by an equal amount, which in effect meant that Dominion was obliged to pay 1 1/2% to 2% more than before and that it would have to increase the price to the consumer in this amount.

At the time, Mr. Jackson stated, Dominion Stores did not delist Kellogg's products; rather, the retailer spoke to other suppliers of cereals which proposed better deals. These negotiations led to the listing of several new products from other suppliers. In order to make room for these products, it was necessary to reduce the listing of Kellogg's products. Even so, only different sizes were eliminated, not different product categories.

In order to be absolutely certain that I received complete and accurate information as to the Kellogg incident, the Commission retained the services of an officer of the Ontario Provincial Police trained in the investigation of such matters. His report confirmed the testimony given in every respect. Consequently, I am satisfied that the explanations given are satisfactory.

(d) Mr. Archie McLaine, is the Vice-President of Marketing for McCain Foods Limited of New Brunswick. Mr. McLaine testified that, over the years, his firm has had products delisted as they were not selling in sufficient volume.

The witness referred to such payments as "inside money," but admitted that, in his opinion, such payments are perfectly legal on the part of the retailer.

EVIDENCE SUPPORTIVE OF DELISTING

(a) The brief of the Retail Council of Canada expressed the view that it is unrealistic for suppliers to expect to be assured of shelf position. Shelf position must depend on a product's performance, in the Council's opinion. Delisting is a rather desirable part of the commercial system because it matches supply and demand.

The Council was critical of the G.P.M.C. survey of 50 suppliers, submitting that the results are meaningless without full information of the circumstances surrounding the delisting. The Council submitted that the delistings could have only minimal effects if limited merely to specific regions or to product or package sizes. It was also submitted that considerations such as lack of volume sales, low profitability or better terms offered by competing products may have applied.

(b) The following supplying and manufacturing firms testified on delisting practices at the Inquiry:

(i) Catelli

(ii) St. Lawrence Starch

(iii) Kellogg-Salada

(iv) Gay-Lea

(v) Kraft

(vi) H.J. Heinz

(vii) General Mills

(viii) Canadian Canners

(ix) General Foods

(x) Canada Starch

(xi) Quaker Oats

(xii) Standard Brands

(xiii) Campbell's Soup

(xiv) Green Giant

(xv) Canada Packers

(xvi) Christie Brown

(xvii) General Bakeries

All of the companies on this roll of names, a roll that includes fifteen members of the G.P.M.C., testified that they had never been delisted due to a retailer demanding a higher rebate. The majority has had products delisted from time to time, usually due to the fact the product was not selling in sufficient volume. Another reason provided was that competitors offer better trade terms causing the present supplier's products to be delisted.

(c) All the major retail chains testified as to this issue and the following is a summary of their evidence pertaining to delisting.

Dominion Stores reviews the sales of its commodity groups on a weekly basis. Products are discontinued for various reasons; during 1978, for example, Dominion Stores delisted 420 products for the following reasons: slow sales (204), metric changes (71), seasonal products (47), one-time purchases (40), products discontinued by supplier (36), package changes (15) and legislation prohibiting certain soft drink containers (7).

Mr. Nichol of Loblaws testified similarly that the major reason for delisting is that a product is not selling. Mr. Nichol insisted that products are not delisted in response to the supplier's failure to meet trade demands.

Mr. Levine of Steinberg's also testified that the major reason for delisting products is that the products are slow sellers. Steinberg's delisted 206 products during the period of January 11 to June 11, 1979. No products were delisted because suppliers did not meet a competitor's rebates, though delistings occur weekly.

A&P, testified Mr. Kennedy, only delists a supplier if the product performs poorly or if the product mix does not warrant it being carried. Furthermore, if A&P relists a product that has been delisted, it does not ask the supplier for a higher rebate as a condition of relisting.

The Oshawa Group, according to the Vice-President of Sales Operations, Mr. Al Graham, discontinues a product when that product's sales velocity no longer earns its place in a warehouse or on the retailer's shelf.

CONCLUSIONS

The following summarizes my conclusions on the evidence examined in this chapter:

1. Listing allowances (also called "introductory allowances") are offered by suppliers to retailers in return for services performed and for risks borne by the retailer upon the introduction of a new product.

2. The amounts paid for such allowances do not appear to be unreasonable considering the cost and risk of new-product marketing to the retailer.

3. The allegation that manufacturers are delisted for failure to meet discounting demands has not been substantiated. The evidence of 24 major food manufacturers and of the major retail chains is, in fact, that products are delisted usually because of poor sales, not for discounting reasons.

4. The G.P.M.C., the manufacturers, and retailers were unanimous in their view that if a problem exists in the listing or delisting of products, it could best be solved in the market place without legislative interference.

CHAPTER 16

REBATES AND THE LAW

INTRODUCTION

The purpose of this chapter is to examine the state of the law pertaining to rebates in Ontario.

Legislation is currently in place to be found in the federal Combines Investigation Act which not only addresses discounting practices but other aspects of competition as well. It was alleged before this Commission by various witnesses that this legislation is unable to prevent the growth and abuse of market dominance by a few major grocery chains. Legislation affecting discounting presently in effect in the United States known as the Robinson-Patman Act was held up as a model for Ontario to follow. In addition, the Ontario Liberal Party and the Ontario Federation of Agriculture proposed draft legislation and made suggestions which the Commission was urged to recommend to the Ontario Legislature.

With this background in mind, I shall deal with the applicable law in three sections. The first section will review the Combines Investigation Act with a view to examining whether or not it is capable of prohibiting business behaviour detrimental to competition, as certain discounting practices are alleged to be. The second section will review the Robinson-Patman Act with a view to examining the effect of this statute on business within the United States. The third section will review the proposals

submitted by the Ontario Liberal Party and the Ontario Federation of Agriculture with a view to examining whether or not this Commission should recommend either proposal, or any variation thereof, as a solution to the problem indicated by the evidence.

It should be made clear that this Inquiry was not primarily concerned with "illegal" discounting practices such as "under-the-table" payments or "kickbacks" paid to individuals in order to obtain certain personal favours. These practices are already indictable criminal offences. It is clear that the Resources Development Committee, the legislative committee whose deliberations were responsible for instituting this inquiry, was not concerned with such dealings. The same point was made clear from the first day of the Commission's hearings where it was clearly stated on the record that kickbacks are not the subject of this Inquiry. Instead, my attention in this report is attracted to practices which may presently be legal but which may have adverse effects in the market place.

A. Present Law in Canada: The Combines Investigation Act*

In this section, I will discuss the law in Canada pertaining to discounting practices. For reasons which will be discussed in section C of this chapter, it is the federal government of Canada which has enacted legislation in this area rather than the provincial governments. I will analyze the sections of this legislation which deal with discounting practices, sections 34 and 35. I will also briefly discuss other sections of the Act with which sections 34 and 35 are integrated in order to protect competition, namely those sections dealing with loss-leader selling and with mergers and monopolies. Finally, I will review the enforcement of the Act.

First, a few words about the Act and its enforcement in general are in order.

The principle underlying the Combines Investigation Act is that the public interest is best served by a market system characterized by fair competition. Consistent with this principle, certain business practices are prohibited which are believed to limit actual or potential competition. Among the practices prohibited are certain discounting practices forbidden in sections 34 and 35 of the Act.

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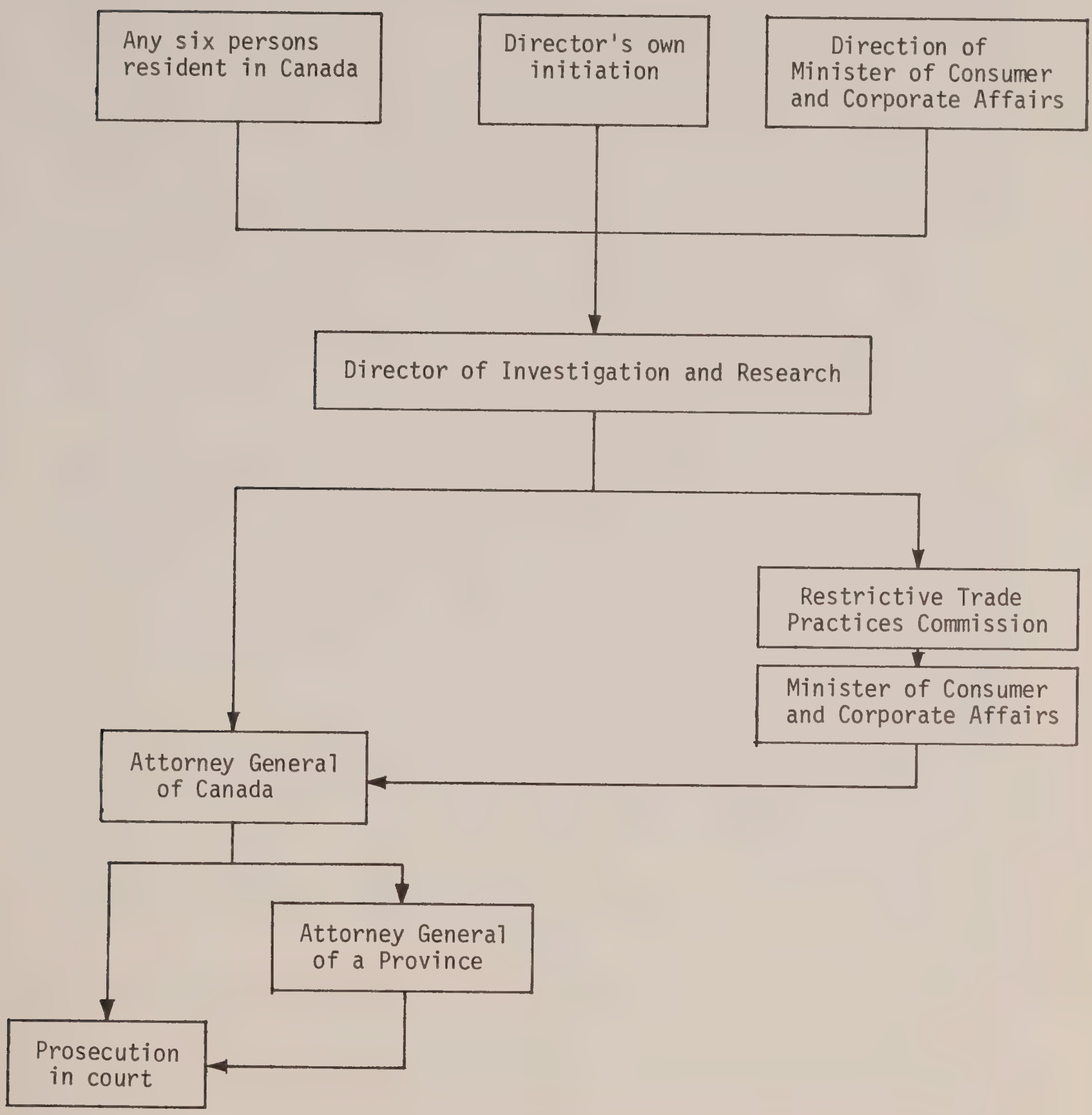
* R.S.C., 1973, c. C-23 as amended.

All investigations under the Combines Investigation Act are conducted initially by the Director of Investigation and Research. An investigation may be set in motion in any one of three ways: 1) any six persons resident in Canada may apply to the Director for an inquiry; 2) the Director may commence an inquiry on his own initiative; or 3) the Director shall cause an inquiry whenever he is so directed by the Minister. See Figure 16-A.

In those instances in which the Director considers that the evidence warrants prosecution rather than discontinuance of the investigation, he may either remit his records to the Attorney-General of Canada who determines whether legal proceedings should be instituted, or he may prepare a statement of evidence for submission to the Restrictive Trade Practices Commission (R.T.P.C.). If the latter route is followed, the R.T.P.C. holds private hearings, evaluates the evidence, and issues a written report to the Minister of Consumer and Corporate Affairs. The Attorney-General then considers the R.T.P.C. report with a view, again, to deciding whether legal proceedings should be instituted. Where the matter is referred to the Attorney-General of Canada, the Attorney-General may institute and conduct the proceedings. Alternatively, an offence may be prosecuted by the Attorney-General of the province who is responsible for the administration of justice in the province under the British North America Act. The matter of enforcement will be dealt with more fully later in this section of this chapter.

FIGURE 16-A

INVESTIGATIONS UNDER COMBINES INVESTIGATION ACT



1. <u>Analysis of Sections 34 and 35 Pertaining to Discounts, Allowances and Rebates</u>

In 1935, the Royal Commission on Price Spreads reported to the federal Parliament that unfair price discrimination, often perpetrated by price concessions in the form of rebates, imperilled the survival of independent retailers. Parliament's response was enactment in the same year of an amendment to the <u>Criminal Code</u> of Canada. This amendment remains a part of our law today as section 34 of the <u>Combines Investigation Act</u> which has undergone only minor drafting changes since the original amendment to the Criminal Code.

In 1958, a study of pricing practices in the grocery trade* reported a concern to the federal Minister of Justice that big buyers used their superior bargaining power to force advertising expenditures upon suppliers in the form of advertising allowances granted by suppliers. These allowances were found to be detrimental to smaller buyers who did not receive proportionately favourable treatment. In 1960, a year after hearing from the Royal Commission on Price Spreads of Food Products which reported the same concern, the federal Parliament enacted another amendment to the <u>Criminal Code</u>. This amendment stands today as section 35 of the <u>Combines Investigation Act</u>.

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* Restrictive Trade Practices Commission, <u>Report Transmitting a Study of Certain Discriminatory Pricing Practices in the Grocery Trade made by Director of Investigation and Research</u> (Ottawa: 1958).

Many of the concerns raised by the federal Commission that reported in 1935 and by the federal Commission that reported in 1959 are essentially the same concerns raised before this provincial Commission.

Evaluation of these concerns and of the appropriateness of the legislative responses require a brief analysis of sections 34 and 35 as they apply to discounting practices.

a) <u>Section 34(1)(a)</u>

Section 34 addresses the offence of discriminatory rebates in paragraph 34(1)(a) to which a defence is provided in subsection 34(2). The section in its entirety is re-printed in Appendix 9. Paragraph 34(1)(c) addresses the practice known as predatory pricing while paragraph 34(1)(b) is simply aimed at a more specific type of price discrimination called "regional (or territorial) price discrimination." I am here concerned mainly with 34(1)(a) and 34(2) since these refer directly to discounting practices. Paragraph 34(1)(c) will be treated more fully at a later point in this section.

Section 34(1)(a) provides:

> "34.(1) Every one engaged in a business who...(a) is a party or privy to, or assists in, any sale that discriminates to his knowledge, directly or indirectly, against competitors of a purchaser of articles from him in that any discount, rebate,

> allowance, price concession or other advantage is granted to the purchaser over and above any discount rebates, allowance, price concession or other advantage that, at the time the articles are sold to such purchaser, is available to such competitors in respect of a sale of articles of like quality and quantity...is guilty of an indictable offence and is liable to imprisonment for two years."

The analysis of this section will proceed by identifying four elements:

(i) the like-quantity requirement,

(ii) the availability requirement,

(iii) the buyer-liability issue, and

(iv) the practice defence.

There are no judicial decisions on the meaning of section 34(1)(a). Nevertheless, an opinion can be formulated as to the elements of the offence based on three sources: 1) the interpretation of the Director of Investigation and Research as revealed in the present Director's testimony before this Commission and in the investigations reported in the Director's annual reports, 2) the interpretation of the Restrictive Trade Practices Commission as expressed in the reports of their decisions, and 3) the interpretation of commentators as expressed in legal journals.

(i) The Like-Quantity Requirement

It is obvious from a reading of section 34(1)(a) that it does not prohibit all rebates, nor does it prohibit different levels of rebates being granted to different customers. For the prohibition to apply, the articles sold must be of "like quality and quantity."

The effect of the "like quantity" proviso is nicely illustrated by the report of the Restrictive Trade Practices Commission on the Pricing Practices of Miss Mary Maxim Limited.*

Mary Maxim, a producer of knitting yarns, classified its department store customers as small stores ("list 1"), small department stores ("list 2"), and "the Big Four" department stores ("list 3"). List 3 customers -- including such firms as the T. Eaton Company, Simpsons Sears Limited, and the Robert Simpson Company -- generally obtained rebates of 42% while list 2 customers received rebates of 40% and list 1 customers between 36% and 38%. The R.T.P.C. found this plan to be discriminatory because rebate levels were not related to differences in volumes purchased. The classifications were admittedly arbitrary; that is, the classification system was not based on actual sales but on sales potential as estimated by the company's staff. It was not the practice of the company to check whether a customer placed on a preferred list on the basis of potential or estimated volume had met the company's expectations.

* R.T.P.C. Report No. 38, 1966, Commissioners: MacLellan, Couture and Eldon.

As a result of the R.T.P.C.'s findings on this issue, proceedings were instituted for an order prohibiting the continuation or repetition of the alleged price discrimination. An order was subsequently granted by the Federal Court in 1968, and the Director's inquiries indicated that the firm adopted a systematic volume rebate schedule thereafter.

On the other hand, Mary Maxim was also alleged to have discriminated against competitors of Eaton's by entering into an agreement with that company alone to grant a rebate of 2 1/2% on the first $380,000 of purchases and 3% on purchases above that amount. The Commission did not find this agreement to be discriminatory because no other customer bought the same volume. In fact, the agreement provided that if another retailer contracted to purchase a greater volume from Mary Maxim, Eaton's would have to agree to increase its purchases so as to remain Mary Maxim's largest customer.

The "like quantity" proviso in section 34(1)(a) recognizes the economies of producing and delivering larger quantities. However, critics of the Act claim the like quantity proviso prevents the section from addressing the concern which prompted the 1935 Royal Commission's recommendations -- the concern that mass buyers' ordering of large quantities places these buyers in a potentially dominant bargaining position.* As we have seen in the Mary

* Notably, Robert Nozick, "The Regulation of Price Discrimination," Canadian Bar Review 54 (1976), p. 309. Also, Bruce Dunlop, "Predatory Pricing and Systematic Delivered Pricing," reprinted in Prichard et al., Canadian Competition Policy (Toronto, 1979), p. 405.

Maxim Case, there is no limit to the difference in rebate levels which a large buyer may demand of its supplier so long as the large buyer buys significantly more of the supplier's product than any other competitor.

Whatever difficulty this proviso may pose for small competitors is somewhat overcome by the legality of certain forms of buying groups. As described in Chapter 7 of this Report, smaller buyers may pool their purchases from suppliers by purchasing jointly through a buying group which qualifies for larger rebates than each member would receive individually. In order to comply with the Combines Investigation Act as currently enforced, such an arrangement must be structured so as to ensure the existence of two transactions: one being the purchase by the group from the supplier and the other being the purchase by the buyers from their group. If, on the other hand, there is only one transaction (for example, if the buying group were to buy on behalf of its members as would an agent), then such a transaction may run afoul of the Act since the individual volume purchased would probably not qualify for the larger rebate.

In testimony before me, the Director of Investigation and Research under the Act indicated that a special requirement might be imposed on a buying group that was in the position of dominating a market. In this case, the Director would discourage the use of exclusionary clauses preventing the admission of potential members. Such a position raises the possible application of sections 32 and 33 which address conspiracies and monopolies.

(ii) The Availability Requirement

A second requirement of section 34(1)(a) is the requirement that rebates be "available." Availability of rebate plans was raised as an issue in testimony by the general manager of a trade association which, nationally, represents approximately 4,500 independent retailers. Although this witness could not refer the Commission to specific evidence or to witnesses who could corroborate his testimony, he asserted that a number of his members were unaware of the variety of allowances offered. Accordingly, he recommended that suppliers to the retail trade be compelled to publish a list showing all terms and conditions of rebates, discounts and allowances to legitimate prospective purchasers.

In testimony before the Commission, the Director of Investigation and Research expressed his opinion that a supplier's keeping discounting terms secret is not only legally prohibited, but is also not sound business practice. The customer who learns that his supplier is favouring other customers but not himself is not likely to continue patronizing that supplier. The current Director's predecessor went further than this in suggesting to the Bar of Ontario that, in most cases, discount schedules or quantity price lists can only be said to be available if they are published.*

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* D.W.A. Henry, "Unfair Distribution and Pricing Practices", Special Lectures of the Law Society of Upper Canada, 1963, p. 43.

On the other hand, the selling company may still preserve the confidentiality of its marketing plans vis à vis its competing sellers. As the R.T.P.C. stated in the Mary Maxim Case, where a supplier provides a rebate on the basis of volume purchased, he is obliged to provide information only to those competing buyers 1) who make inquiry, and 2) who show reasonable prospect of being able to purchase like volume. Once both these conditions are satisfied by the buyer, however, the seller must provide that buyer with all the information about the rebate including the level of purchases required to be eligible for a rebate, the amount of the rebate, the manner in which the rebate will be applied and the manner in which it will be paid.

(iii) The Buyer-Liability Issue

A third aspect of section 34(1)(a) which attracted attention was whether or not buyers are liable. The two federal Royal Commissions whose recommendations prompted price discrimination legislation in Canada both identified the "culprit" as being the big buyer as typified by the chain supermarket. It would be ironic, then, if the legislation designed to remedy the situation imposed liability on the seller alone, particularly if it is the buyer's market power which supposedly forces the supplier to grant price concessions. Yet the Grocery Products Manufacturers of Canada criticized the law for failing to impose liability on the buyer and recommended that the Act be amended to ensure that purchasers would be directly responsible if they knowingly receive discriminatory rebates.

Admitting that his office's interpretation has been disputed in the legal literature,* the Director of Investigation and Research submitted that buyer liability is already a feature of the Act and that his enforcement would proceed on this premise. The Director's interpretation is derived from the words in section 34(1)(a): "Everyone engaged in a business who...is a party or privy to, or assists in, any sale that discriminates to his knowledge...." These words reappear in the advertising allowance section, 35(b): "Everyone engaged in a business who is a party or privy to the granting of an allowance to any purchaser that is not offered on proportionate terms...."

The word "party" is defined in section 21 of the *Criminal Code* as being a party to any offence. It is also possible that a buyer might be prosecuted under sections 22 and 422(a) of the Code for counselling the seller to commit an offence. These sections, in addition to the definition of the word "party" found in section 21 of the *Criminal Code* are repeated in full in Appendix 9.

Applying criminal law principles, I should remark that buyer's liability depends further on the presence or absence of *mens rea*, or criminal intent. The Director has suggested that the requisite intent in this case is the buyer's knowledge that other competing buyers are not receiving equivalent rebates. Accordingly, it does not appear to be an offence for the buyer to insist on a better

* See Nozick, *op.cit.*, at p. 309.

rebate, though it is an offence for the buyer to insist that he receive a better rebate than competing buyers are receiving. This is illustrated in the following exchange between Commission Counsel, Mr. Hull, and the Director of Investigation and Research, Mr. Bertrand (Transcript: Vol. 43, p. 29):

> "MR. BERTRAND: ...[If the buyer says,] '[w]e want [a] ten percent discount and two percent more than your nearest buyer, irrespective...[w]e want two percent more or X percent more than anybody else or else we don't do business with you...'
>
> MR. HULL: It's an offence.
>
> MR. BERTRAND: This could be prosecuted....
>
> MR. HULL: But if you say, I see the ten percent, you better sharpen your pencil, that's not an offence?
>
> MR. BERTRAND: It is not...."

Several retailers apparently share the Director's interpretation that, as buyers, they could be equally liable for the supplier's contravention of section 34(1)(a) or section 35. Dominion Stores, Loblaws, A & P and Safeway all make suppliers sign a warranty to the effect that the rebates received are made available to like customers. A sample of such a warranty is provided in Appendix 8 of this Report. In the Director's opinion, the legal effect of this warrranty is to protect the corporation from the unauthorized action of its individual buyers; it is not

conclusive evidence of the company's innocence and could be overcome by evidence to the contrary.

(iv) <u>The Practice Defence</u>

The fourth aspect of section 34 worthy of mention here is the defence provided in section 34(2) applicable to price discrimination under 34(1)(a). Section 34(2) reads:

> "(2) It is not an offence under paragraph (1)(a) to be a party or privy to, or assist in any sale mentioned therein unless the discount, rebate, allowance, price concession or other advantage was granted as part of the practice of discriminating as described in that paragraph."

Because discrimination must be a practice before there is an offence, the firm accused may try to describe its conduct as a "temporary expedient." For example, the supplier may say it discounted because it was necessary to meet spot competition. For another example, the supplier may say it discounted in order to get rid of excess inventory.

What constitutes a "practice" as opposed to a "temporary expedient" must be decided in each case as there is no clear-cut test that can be applied. While a rebate granted to one retailer and not another for a period of four months might be discriminatory, a rebate granted for a period of

three months during a price war might not be discriminatory.*

The "practice" defence has been viewed by some as a severe limitation on the effectiveness of section 34(1)(a). Simply because the discrimination is temporary does not, in my view, necessarily make it less harmful. For example, if the discrimination occurs during a price war when buyers are very price sensitive, an isolated act of discrimination such as a spot price reduction may have disastrous consequences on those discriminated against.

On the other hand, the practice defence is justifiable in that it obliges the enforcement agency to consider the competitive significance of the discriminatory conduct.

b) Section 35

As indicated in the history recited earlier, section 35 of the Combines Investigation Act was intended to complement section 34(1)(a) by dealing with a special type of rebate -- the advertising and promotional allowance. The 1958 Study of Discriminatory Pricing Practices concluded that, because it refers to the sale of articles, section 34(1)(a) does not apply to purchases of advertising and promotional services. The study also concluded that buyers of smaller quantities would be best protected if the law

* Report Concerning Distribution and Sale of Gasoline in the Toronto Area: Alleged Price Discrimination-Supertest Petroleum Corporation Ltd., R.T.P.C. #13, Commissioners: Smith, Carginan, Whitely, 1961.

ensured that they would receive proportionately equal treatment in respect of advertising allowances.

Section 35 is printed in full in Appendix 9 and only the prohibitory paragraph, 35(2), is reprinted here for ease of reference.

> "(2) Every one engaged in a business who is a party or privy to the granting of an allowance to any purchaser that is not offered on proportionate terms to other purchasers in competition with the first-mentioned purchaser, (which other purchasers are in this section called "competing purchasers"), is guilty of an indictable offence and is liable to imprisonment for two years."

Paragraph 35(1) defines the term "allowance." Paragraph 35(3) defines "proportionate terms."

The key to understanding section 35 is the concept of "proportionality." According to the federal authorities, section 35 requires that every advertising and promotional allowance be given in the same proportion to competing purchasers. For example, if a supplier gives a 5% promotional allowance to a major chain, it must also offer a 5% promotional allowance to the smaller retailer.

It is worthy of note that the proportion offered or given depends on the value of the sales, not on the value of services. Thus, it is not a defence for the supplier to say that the major chain was offered $50,000 for a

television advertisement, but that the smaller retailer was offered nothing because the smaller retailer could not provide television advertisement. Following the same example, if the major chain was granted an allowance of $50,000 on $1,000,000 sales, then the smaller retailer must be offered $500 on $10,000 sales. While the manufacturer and his large retail customer may agree on a $50,000 television advertisement, the manufacturer and his small retail customer may agree that the $500 should be spent on window display signs. However, agreements as to the value of differing forms of promotion are often very difficult to reach in practice as was indicated in the Brief of the Grocery Products Manufacturers of Canada.

2. Descriptions of Other Sections Protecting Competition

As we have seen, section 34(1)(a) and 35 are designed to protect competition, especially small business, from discrimination. The small business has other provisions in the Combines Investigation Act that it may rely on as well, most notably section 33 prohibiting mergers and monopolies, and section 32 prohibiting conspiracies. Retailers and wholesalers are afforded protection against suppliers' refusals to deal with them pursuant to section 31(2). Suppliers may generally not require a customer, as a condition of supplying a product, to deal only in their products or to refrain from dealing in competing products, or to acquire some other product from them, or to sell a product only in a defined market, pursuant to section 31(4). Suppliers may not direct retailers as to how the latter must price their products, pursuant to section 38.

These sections will not be discussed further than to mention them as sources of protection for small business and for businessmen generally.

Two other sections of the Act have drawn more considered attention because they deal with two issues raised in this inquiry. These are the issues of a) loss-leader selling, and b) mergers and monopolies.

The relevance of loss-leader selling is discussed in Chapter 14; briefly, loss-leader selling may result in retail pressure on suppliers for price reductions. The relevance of mergers and monopolies is discussed in Chapter 12. Similarly, the concern is with the kind of market pressure that may lead to increased discounting.

a) Loss-Leader Selling

Loss-leader selling is not presently prohibited *per se* by either Ontario law or federal law. However, loss-leader selling may constitute "predatory pricing" so as to contravene section 34(1)(c) of the *Combines Investigation Act*.

Section 34(1)(c) is set out below:

> "34.(1) Every one engaged in a business who...
> (c) engages in a policy of selling products at prices unreasonably low, having the effect or tendency of substantially lessening competition

> or eliminating a competitor, or designed to have such effect...is guilty of an indictable offence and is liable to imprisonment for two years."

Paragraph 34(1)(c), the predatory-pricing paragraph, differs from paragraph 34(1)(a), the discriminatory-pricing paragraph, in that paragraph (a) does not apply to consumers. A reading of paragraph (a) indicates that it refers to purchasers who are engaged in a business and who are engaged in resale. Paragraph (c) is not similarly restricted; it may apply to suppliers selling to the retail/wholesale trade or to retailers selling to consumers. In this report, when I refer to "loss-leader selling," I am referring to the latter transaction concerning sales to consumers.

I will now examine the requirements of section 34(1)(c). I will then turn to legislation in other jurisdictions affecting loss-leader selling to which I have been referred.

i) Requirements of Section 34(1)(c)

The following elements of section 34(1)(c) are worthy of note: 1) the policy requirement, 2) the competition requirement, and 3) the "unreasonably low price" requirement.

The use of the word "policy" in paragraph 34(1)(c) is similar to the use of the word "practice" in subsection 34 (2) and the same considerations as discussed above probably apply to this section as well. To reiterate, spot price cutting is probably not a "policy" and thus would be legal. Likewise, loss-leader selling engaged in for a particular reason such as excess inventory, a store-opening, a new product promotion, or perishable merchandise would probably not be illegal. Nor is loss-leader selling with the intention of meeting a competitor's price, which sometimes escalates into a price war, likely to be found offensive subject to the qualification of the competition requirement explained in the next paragraph.

Paragraph (c) imports a test which is not present in paragraph (a): that of 1) having the effect or tendency of substantially lessening competition or eliminating a competitor, or that of 2) being designed to have such effect. Thus, the practice of loss-leader selling by the firm with a large market share, if engaged in for sustained periods of time with the purpose of disciplining competitors or forcing them to withdraw from the market, or, if designed to have such an effect, could very well be an indictable offence. However, the loss-leader seller's purpose or intent is admittedly easier to state than to prove as is indicated by a case recently decided by Mr. Justice Linden of the Supreme Court of Ontario, <u>Regina</u> v. <u>Hoffman-LaRoche Ltd</u>.*

* S.C.O., Linden, J., Judgment Released: February 5, 1980, decision as yet unreported.

In The Hoffman-LaRoche Case, the accused, a manufacturer and distributor of pharameceutical products, was convicted of selling the drug Valium free to hospitals for the period of one year. In considering the competition requirement, the court held that effect or tendency could not be proved because the tiny share of the market held by the accused's competitor was not "substantially lessened," because the proportion of the competitor's hospital sales did not vary during or after the giveaway period, and because no competitor was eliminated from the market as a result of the giveaway.

However, the giveaway was designed to have the requisite effect as evidenced by intra-corporate documents expressing the accused's desire to eliminate competitors and lessen competition. Memoranda spoke of "aborting" efforts of competitors and of "teaching a lesson" to them. Roughly speaking, the company was convicted because it engaged in loss-leader selling designed to be injurious to competition.

Section 34(1)(c) also requires that pricing be "unreasonably low" before it is offensive. In his Hoffman-LaRoche decision, Mr. Justice Linden neatly sets out the considerations critical to deciding whether or not a price is "unreasonable" (at pages 73 to 75):

1) the greater the reduction below cost, the more likely the price is unreasonable;

2) the length of time during which the sales take place -- the longer the deal lasts, the more suspect it becomes;

3) the circumstances of sale, particularly whether prices are reduced in response to or in advance of competitors' price reductions.

4) the economic benefits accruing to the seller including later advantages which may accrue.

Therefore, simply selling below cost is not an offence. This requirement is also complicated by the difficulty in calculating "cost" which may include costs of manufacture, delivery, shelving and sale.

To summarize what has been said about the requirements of section 34(1)(c), loss-leader selling seems to be a perfectly legal method of competition under the Combines Investigation Act. Suspicion arises, however, when a market-dominant firm severely reduces prices over a protracted period of time with the intent of injuring competition.

(ii) Loss-Leader Selling in Other Jurisdictions

Legislation in other provinces affecting loss-leader selling has been brought to the Commission's attention. The province of British Columbia prohibits recipients of milk and manufactured milk products from selling or offering the same for sale at a price below cost.* The

* The Milk Industry Act, R.S.B.C., c. 293, s. 57.

provinces of Alberta,* Saskatchewan,† Quebec,** Nova Scotia,†† and New Brunswick*** have vested authority in various boards and commissions for the purposes of establishing minimum retail prices for milk.

In the province of Manitoba, the government may, by regulation, vest in any producer, board, or marketing commission, the power to fix minimum prices at which products may be sold at any marketing level.††† It is worthy of note that such sweeping power has not been exercised to date to prohibit loss-leader selling by retailers.

In Quebec**** and New Brunswick,†††† minimum price legislation applies to the sale of bread. Furthermore, any mention of the price of bread is prohibited other than on the package or on the display counter used for sale. This is aimed at the practice of using loss-leader selling as an advertising tool to induce customers to come into the shop. The effects of this legislation are discussed in Chapter 13 on loss-leader selling.

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* The Dairy Board Act, R.S.A., 1970, c. 234 as amended, s. 12.

† The Milk Control Act, R.S.S., 1965, c. 234 as amended, s. 7(c)(d); also see Order No. 522, s.2.

** Dairy Products and Dairy Products Substitutes Act, S.R.Q., 1969, c. 45, ss. 13,14.

†† Distribution and Sale of Milk Act, 1968, s. 177.

*** Dairy Products Act, c. D-2, ss. 4(c), 15(1)(2).

††† Natural Products Marketing Act, s. 32.1.

**** An Act Respecting the Bread Trade, S.Q., 1974, c. 34, s. 2; also see Regulation 73-599, s. 5.

†††† An Act Respecting the Bread Trade, s. 2; Regulation Respecting the Bread Trade, s. 3.

In Canada, then, the legislation of certain provinces establishes minimum retail prices for certain commodities, usually after consideration of processors' and retailers' cost data. In the United States, the State of California has enacted legislation expressly prohibiting loss-leader sales of any commodity. In the *Unfair Practices Act*,* "loss leader" means any article or product sold at less than cost for the purpose of enticing the purchase of other merchandise, for the purpose of misleading or deceiving purchasers or where the effect is to injure competitors.

In considering legislation such as the California legislation, I take the view that if the criterion for liability is injury to competitors, rather than injury to competition, the wrong test is being used. As indicated previously, there seems to be nothing remiss in a retailer with a small percentage of market share using the marketing device of loss-leader selling in order to take customers away from a retailer with a dominant percentage of market share. In this instance, loss-leader selling might injure a competitor (the market-dominant retailer) but it may equally promote and enhance competition to the consumer's benefit.

b) *Mergers and Monopolies*

Like the issue of loss-leader selling, the issue of mergers and monopolies is concerned with market pressure and the extent to which the retailer is able to oblige a

* *California Laws of 1941*, c. 526, as amended.

given supplier to offer rebates. As to this issue, it was alleged that the Ontario retail food market is in danger of being controlled by a monopoly of one, or an oligopoly of two or three, major chain(s). The practical probability of this occurrence is treated in Chapter 13, Concentration and Rebates; this section will briefly examine the legal possibility.

There is another reason why this area of the law is of interest. The province's leading food retailer, Dominion Stores Limited, suggested that if there were to be legislation limiting rebates, then retailers would seriously consider increased vertical integration by way of response. In this manner, a retailer would avoid the sale transaction required by sections 34 and 35. Therefore, I think it necessary to briefly consider whether a major retailer such as Dominion Stores could legally integrate vertically by merging with suppliers, that is, by purchasing shares or assets of supplying corporations.

It is an offence to be a party to or privy to, or to knowingly assist in, the formation of a merger or monopoly pursuant to section 33 of the Combines Investigation Act. As defined by section 2 of the Act, mergers are prohibited if competition is, or is likely to be lessened to the detriment or against the interest of the public; similarly, monopolies are prohibited if they operate or are likely to be operated to the detriment or against the interest of the public. The texts of these sections are re-printed in Appendix 9.

As I explained in Chapter 13, many economic theorists predict that monopolistic and oligopolistic markets will have an adverse effect on the economy: that consumers must pay higher prices and that producers will be paid lower prices than would prevail in a more competitive market.

The courts, on the other hand, do not seem to be satisfied with such a prediction and will not presume that control or domination of a market structure is detrimental to the public interest. They require proof that the monopoly or oligopoly conducts itself or performs in a detrimental manner.

For example, in the Breweries Case,* the accused company controlled 60.9 percent of the market after merging with 37 competing breweries. In the Sugar Case,† the only sugar refiner in the provinces of British Columbia and Alberta purchased the only sugar refiner in Manitoba, leaving the former as the only sugar refiner in the western provinces. In the K.C. Irving Case,** the accused companies accounted for 97% of English-language daily newspapers purchased in the province of New Brunswick. In each of these cases, monopolistic or oligopolistic market structures seemed to be proved to the satisfaction of the court. In none of these cases was the accused company convicted, however, because it was not proved to the satisfaction of

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* Regina v. Canadian Breweries Ltd. (1960), O.R. 601 (McRuer, C.J.H.C.).

† R. v. British Columbia Sugar Refining Co. Ltd. (1960) 32 W.W.R. 557 (Manitoba Court of Queen's Bench, Williams C.J.Q.B.).

** R. v. K.C. Irving, et al (1978) 1 S.C.R. 408.

the court that the oligopoly in question performed in a detrimental manner.

The Director of Investigation and Research, responsible for enforcing the merger and monopoly provisions, is of the opinion that these court interpretations make his task difficult. In order to find actual detriment, "what the court has concluded is that you must find bodies lying around." "Bodies" (firms forced out of the market) must be attributable to the merger, not to any other factor. The Director testified that in order to find potential detriment, according to the criminal law, "it has to be more than a possibility of detriment. It has to be a probability of detriment" proved beyond a reasonable doubt. "So in practice, it turns out that the merger provision is very difficult to enforce under criminal law."

This interpretation of the merger and monopoly sections has not prevented the Director's office from inquiring into two situations involving food retailers: one relating to the Weston purchase of Loeb stock and the other relating to Canada Safeway.

In 1973, it was reported in the press that George Weston Limited, the parent corporation of the major food retailer Loblaws Limited, had acquired more than 20% of the voting stock of M. Loeb Limited, a partner in the IGA food retail franchise; consequently, there was concern that food distribution competition would be lessened and that much of the business conducted by Loeb with non-Weston suppliers would be lost. Accordingly, the Director commenced an

inquiry which was terminated following a formal undertaking by Weston to dispose of its stock interest in Loeb as soon as possible. Loblaws also undertook to refrain in the meantime from exercising its influence on the management of Loeb or from voting shares in any Loeb shareholder meeting. In fact, Weston disposed of its interest in Loeb at the time of the latter's purchase by Provigo Incorporated in 1978.

Canada Safeway Limited was charged before the Supreme Court of Alberta with formation of a monopoly prohibited by section 33, a situation which is more fully described in Chapter 13. Ultimately, the accused filed a Statement of Admissions which led to a prohibition order consented to by the company in order to avoid lengthy and expensive litigation. It was emphasized by Crown Counsel that the admissions did not involve evidence relating to excessive profits or prices but rather to Safeway's actions limiting the expansion and creating barriers to the entry of competitors.

The Safeway case is consistent with my analysis of the jurisprudence that it is essential to prove monopolistic conduct -- for example, creating barriers to entry -- and that it is not sufficient to prove monopolistic structure as evidenced by a high percentage of market share.

I now return to the original question. It appears that the present legislation, as interpreted by the courts, would not prevent one, two, or three major food retailer(s) from controlling a large percentage of the Ontario retail

food market, subject to the qualification that they did not exhibit monopolistic conduct as well.

However, to say that an event could legally happen is not equivalent to saying that it could practically happen. The very witness who expressed the fear that two or three food retailers might take over the Ontario market also expressed the view that Ontario would never let this happen. I agree in thinking that such a scenario affecting this vital activity would stimulate both provincial and federal interest, and quite possibly, intervention.

For reasons expressed in Chapter 13 on concentration, I think it unlikely that the Ontario retail food market will fall into the control of a very few firms in the near future. To be sure, the statistics indicate that a substantial percentage (approaching 50%) is already in the hands of only two retailers -- Dominion Stores and Loblaws -- and that a still larger percentage (approximately 60 to 70%) is controlled by only five major chains. However, the remaining share of market is, I think, securely in the hands of retailers not affiliated with these chains, so securely as to make improbable any take-over by the larger competitors.

3. <u>Enforcement of the Combines Investigation Act</u>

In the above analysis of selected sections of the competition legislation, I have examined one aspect of the law: its interpretation. It remains to examine a second aspect equally important: its enforcement. I will now do

this against the background of the allegation made before us that the Act is vacuous and generally ineffective.

I have already briefly traced the path of a complaint concerning the Act. It should be stressed at this point that neither of the federal appointees under the Act, being the Director of Investigation and Research and the Restrictive Trade Practices Commission, has the power to regulate discounting practices or any of the other criminal acts, including predatory pricing and monopolies and mergers, prohibited by the Act. The Director's power is one of investigation as to whether particular acts or situations reflect a breach of prohibitions in the Act. To this end, the Director employs a staff of 100 professionals -- trained in economics, business administration and law -- assisted by two branches of the Bureau of Competition Policy, employing 33 professionals each, and from time to time, by officials from the staff of the Department of Justice.

Eventually, the matter may come into the hands of the Attorney General, who considers the Director's records or the R.T.P.C.'s report with a view to deciding whether a prosecution should be instituted.

In fact, only one conviction has been recorded under section 34 or section 35 of the Combines Investigation Act. In Regina v. Rubbermaid (Canada) Limited (1974), the company pleaded guilty to five counts under section 35 and was fined $3,000 on each count. The prosecution obtained a prohibition order in the Mary Maxim Case under section

34(1)(a) as noted previously. One commentary* points out that for the entire time period 1960/61 to 1974/75, there were only five price-discrimination and predatory-price complaint files opened which proceeded to prosecution. This lack of complaints and convictions is consistent with the criticism that the legislation is vacuous and generally ineffective.

This criticism is also supported by the evidence of a representative from one of the five major dairies in the province, Borden Company Limited. This representative testified that his company increased the discount paid to one convenience store retailer from 5% to 15%, although the retailer purchased no more milk from the company than she had purchased previously. When asked by Commission Counsel whether the company's discount practices "stayed within the four corners" of the statute, the representative candidly responded: "Not necessarily...because it is a very competitive world. I think we do, you do what you have to within a competitive situation in your marketplace."

On the other hand, testimony from representatives of more than 24 major nation-wide suppliers indicated that they were well aware of the statute's requirements and indicated, furthermore, that their companies' policies complied fully with these requirements. Many of these witnesses submitted their companies' rebate and price

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* Paul K. Gorecki and W.T. Stanbury, "Canada's Combines Investigation Act: The Record of Public Law Enforcement, 1889 - 1976", in Prichard et al, <u>Canadian Competition Policy</u>, (Toronto: 1979) p. 135, at p. 185.

schedules to the Commission either for the Commission's use on a confidential basis or for public perusal as exhibits.

The Commission is aware that such testimony could be cynically viewed as self-serving and should not be taken at full value. However, it must be remembered that witnesses called before the Commission gave testimony under oath, and that the penalty for perjury is a criminal record and possibly, imprisonment. In addition, there is other evidence leading me to have more confidence in the Act's effectiveness than was expressed in the allegations.

Discovering and prosecuting offenders in the courts is only one way of enforcing the Combines Investigation Act. Another way of preventing the commission of offences is through the Program of Compliance. The Program of Compliance permits businessmen to meet with the Director of Investigation and Research and his staff to discuss either general matters of mutual interest or the Director's response to particular courses of action proposed by a businessman. When it comes to the Director's attention that a firm might have a price structure which violates section 34, the Director informs the firm whether or not a formal inquiry would be recommended based on the information given to the Director. This affords the firms the opportunity to design a new rebate structure which would not contravene this section. The Director's statistics indicate that between 1960 and 1976, a total of 436 compliance requests in relation to price discrimination and predatory pricing were received by his office, a figure which

represents 48.9% of all compliance requests not related to misleading advertising during that time period.*

Under the Act as recently amended,† private enforcment is available to any person who has suffered loss or damage as a result of conduct that is contrary to section 34(1)(a) or section 35, pursuant to section 31.1. This section has only been in force since 1976. Accordingly, its implications and even its constitutionality are not clear. Nevertheless, its potentiality as an enforcement tool should be noted. Reliable testimony of an expert witness from the United States indicates that private enforcement is more of a deterrent than public enforcement in the United States.**

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* Annual Report - 1968/69, p. 17, as cited in Gorecki et al, op. cit., at p. 193.

† S.C., 1974-75-76, c. 76, s. 12.

** Paul LaRue, Transcript Vol. 42, pp. 9, 10.

B. Present Law in the United States: The Robinson-Patman Act*

As we have seen in the last section, the Combines Investigation Act prohibits certain discounting practices in Canada. The extent to which the Act is controlling these practices has been investigated. I now turn to more strict legislative alternatives in this section and the next. In this section, I begin by examining an alternative which has been tried by another country with a food industry similar to our own, the United States. I refer to the Robinson-Patman Act which, like our Combines Investigation Act, is federal legislation.

The Robinson-Patman Act has been in force for 45 years. There is also legislation in Australia which affects discounting, Section 49 of the Trade Practices Law.† This section is derived from the Robinson-Patman Act. The law was only enacted in 1974 so there is little judicial interpretation of its meaning. For these reasons, I have decided to devote my attention to the Robinson-Patman Act rather than to the Australian legislation.

The sources of our information on the Robinson-Patman Act are diverse. The Commission received testimony from an eminently qualified U.S. attorney practicing in this field, Mr. Paul LaRue, as well as from high-ranking officials from the Federal Trade Commission, a government agency charged with the Act's enforcement. Many members of the food

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* Passed June 19, 1936, c. 592, 49 Stat. 1526.
† 1974, c. 51.

industry have had experience with the Act and testified as to its effect. In addition, Commission staff interviewed experts and attended a seminar on this legislation in the United States. There is a compendious body of legal and economic literature on the subject; the Commission's readings are contained in the bibliography provided in Appendix 10.

What was discovered after all our research is that opinion in the United States is widely divergent on the effect which the Act has upon business, and particularly upon competition. This section will outline the reasons for the praise, reservations and criticism with a view towards determining whether Robinson-Patman is a model for legislation which Ontario should enact.

First, a brief history and description of the Act is in order. Then, I will examine how the Act is enforced. Finally, I will advance a critical view of the Robinson-Patman Act together with my recommendation in this regard.

1. History and Description of the Robinson-Patman Act

i) History

The Robinson-Patman Act, like section 34 of our Combines Investigation Act, was enacted during the Depression at a time when small retailers felt threatened by the growth of the large retail food chains. An investigation by the Federal Trade Commission disclosed the chain store

buyers' frequent practice of extracting from suppliers special terms including rebates. These practices permitted chain supermarkets to sell at prices lower than smaller food stores, destroying the competition these small stores provided and ultimately driving them out of the market, in the investigators' opinion.

In order to remedy this situation, the Robinson-Patman Act was enacted as an amendment to section 2 of the Clayton Act* which already prohibited certain discounting practices. The description that follows describes section 1 of the Robinson-Patman Act which is conventionally known as "section 2" because of its place in the Clayton Act. I will adhere to this convention.

ii) Price Discrimination Offence

Section 2(a) of the Robinson-Patman Act makes unlawful discriminations or differences in price by a seller in the sale of like products to two or more competitors. One distinction between the offence created by the American law and the offence created by section 34 of the Canadian law is that the American prohibition requires injury to competition. Under Canadian law, injury to competition is a consideration for predatory pricing and merger and monopoly offences but not for price discrimination offences. However, this distinction between American and Canadian law is considerably diminished by the American courts' interpretation of this section.

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* 38 Stat. 730 (1914).

The American courts have held that, as between retailers, injury to competition can be inferred from the fact of a mere price difference at the retail level.* For example, if a manufacturer of salt sells this product to a chain supermarket at a net price substantially cheaper than prices to other retailers, injury to competition among retailers may be inferred if the chain supermarket then sells the salt to consumers at a price considerably cheaper than its competitors. This inference may be made even though salt is only one of the many products sold by the retailers and arguably has little effect on competition between retailers. Thus, little or no proof is required that the unfavoured customer actually lost business or that trade was actually diverted from the unfavoured to the favoured customer.

Therefore, the offence of price discrimination is relatively easy to prove. It remains to be considered whether the defences are equally easy to prove.

iii) <u>The Cost-Justification Defence</u>

Another difference in the offences created by the statutes is that only "articles of like quality and quantity" are affected by the Canadian section while the American equivalent reads "commodities of like grade and quality." The extent to which different quantities are exempted is discussed below.

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* <u>F.T.C.</u> v. <u>Morton Salt</u>, 334 U.S. 37, 47 (1948).

The cost-justification proviso in section 2 of the Robinson-Patman Act is set out below:

> "2(a)...Provided, That nothing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered."

The cost-justification proviso explicitly recognizes that a seller's cost of dealing with customers who buy in different quantities may vary. The most obvious source of a cost-justification defence arises when a purchaser orders a large quantity of merchandise in such a way as to save costs of production and delivery. It can be said that these savings are equally recognized in the "like quality and quantity" requirement of the Combines Investigation Act, section 34(1)(a). The difference is that the American cost-justification proviso limits the difference in price to the amount of cost saved whereas the Canadian "like quality and quantity" requirement implies no such limitation.

In American law, the burden of proving that a price discrimination is cost justified lies on the defendant who raises the cost-justification defence. The defendant must prove justification by undertaking a cost study conforming to the requirements of the law as interpreted.

These interpretations render the cost-justification defence very expensive. They require an allocation of costs between different customers and different product lines according to historical costs, rather than according to estimated future costs. This allocation must comply with a specified form that is not usual business practice. Interpretations also severely limit the area in which cost savings are recognized. Very accurate computations are required. The defendant often has to retain not only accountants, economists and management consultants but also legal staff in order to meet these requirements.

The Commission heard expert testimony that it is not common practice for firms to perform a cost-justification study prior to revising price structures.* This is because of the expense involved in such a study. Another reason is that the studies are of limited value, based as they are on exact historical costs, whereas a firm planning a revision in its price structure is more interested in future estimated costs. Furthermore, the Robinson-Patman action might occur three years after the cost study has been conducted when conditions have changed.

Another drawback of the cost-justification proviso is that buying groups which merely consolidate members' purchases for ordering purposes and which do not accept delivery, are usually unable to meet the cost-justification requirement.* This description would fit many buying groups currently operating in Canada.

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* As was the case in Alhambra Motor Parts Inc., 68 F.T.C. 1034 (1965).

It has been observed that the threat of having to perform a Robinson-Patman cost-justification study would probably deter suppliers from considering a revision of prices downward in order to account for lower costs of servicing some customers even if the revision is justifiable. If this is the case, then consumers are not well served by such a law.

iv) Other Defences

We have seen that cost justification provides a limited defence to price discrimination prohibited under section 2 of the Robinson-Patman Act. A second defence provided under this section is that price changes may be made in response to changing conditions affecting the marketability of the goods concerned. This defence makes allowance for the deterioration of perishable goods, the obsolescence of seasonal goods, distress sales and sales occasioned by the discontinuance of business in the goods concerned. It is submitted that these conditions would also constitute a defence in Canadian law. As discussed above, rebates granted under such conditions would probably not constitute a practice; thus, a valid defence could be raised under section 34(2) of the Combines Investigation Act.

A third defence to price discrimination is provided in section 2(b) of Robinson-Patman quoted below:

> "2(b)...Provided, however, That nothing herein contained shall prevent a seller rebutting the

prima-facie case thus made by showing that his lower price or the furnishing of services or facilities to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor, or the services or facilities furnished by a competitor."

This defence is known as the "meeting competition" defence and it means that a seller charged with price discrimination can exonerate himself by showing that he was merely meeting a competitor's equally low price.

It seems that the same defence can be raised in Canadian law, again on the basis that the rebate or other advantage was not granted as part of the practice of discriminating, but only as a "temporary expedient." As interpreted, however, the American proviso contains important limitations:

1) the defendant is entitled "to meet, but not beat" its competitor's price;*
2) competition can only be met in specific individual transactions rather than in revision of an entire pricing system;†

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* National Dairy Products Corp., 70 F.T.C. 79 (1968), aff'd, 395 F. 2d 517 (7th Cir.), cert. denied 393 U.S. 977 (1968).

† Knoll Int'l Inc., [1970 - 1973 Transfer Binder] C.C.H. TRADE RED REP. 11 19,768 (FTC 1971), Standard Motor Products, Inc. v. F.T.C., 265 F. 2d674 (2nd Cir.), cert. denied, 361 U.S. 826 (1959), Surprise Brassiere Co. v. F.T.C. 406, F. 2d711 (5th Cir. 1969).

3) the defence is available only to a seller attempting to retain present customers and not to one seeking to acquire new customers.*

The Canadian defence has never been adjudicated so that it is difficult to say what limitations will be placed on the "practice" defence. Cases considering the similar word "policy" in section 34(1)(b) of the Canadian statute suggest that such a defence will have broader scope than its American equivalent.†

v) Illegal Advertising and Promotional Allowances

Sections 2(d) and 2(e) of the Robinson-Patman Act, repeated in the Appendix, make it unlawful for a seller to grant promotional payments, services or facilities for the benefit of a customer unless the same are made available on proportionally equal terms to all customers who compete in the resale of the goods. The Combines Investigation Act, section 35, amounts to the equivalent offence in Canadian law.

In order to assist businessmen in the United States to comply with the law as interpreted, the Federal Trade

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* Sunshine Biscuits Inc., 59 F.T.C. 674 (1961), rev'd, 306 F. 2d 48 (7th Cir. 1962); Standard Motor Products, Inc. op. cit.

† Regina v. William B. Coutts Co. Ltd. (1968), O.R. 549 (Ont. High Court Appeal to Oct. CA dismissed on this issue); R. v. Carnation Co. Ltd. (1969) 4 D.L.R. 3d 133; [1970] 3 Can. C.C. 190 (Alta S.C., App. Dir).

Commission has published guidelines.* My Commission has heard testimony that these guidelines are too complex and too detailed. However, I sympathize with the F.T.C.'s attempt to describe a law that is very complicated. I can well imagine that it would be difficult to design a promotion that is commercially practicable for both a nationwide supermarket chain and a corner grocery store.

One interesting difference between American and Canadian law involves the interpretation of "availability." It will be remembered that in Canadian law this issue arises under section 34(1)(a). Under that section, a supplier must provide information as to rebate schedules only to those competing buyers who make inquiries. Under the Robinson-Patman Act, section 2(d), the supplier must not merely be willing, if asked, but must take affirmative action to inform customers of the availability of promotional programs (Alterman Foods, Inc. v. F.T.C., 497 F. 2(d) pp. 993, 1001 [5th Cir. 1974]). The defence of "availability" does not change the obligation on the supplier, under both Canadian and American law, to offer promotional allowances in the same proportion to competing customers and to ask for promotional services within the economic reach of the competing purchasers.

* Federal Trade Commission, Guides for Advertising Allowances and Other Merchandising Payments and Services ("Fred Meyer Guidelines"), Promulgated May 20, 1969, as amended.

vi) The Buyer Liability Issue

We have seen that the liability of a buyer who induces or receives a discriminatory price is somewhat in doubt in Canada. This doubt does not exist in the United States. The Robinson-Patman Act provides:

> "2(f) That it shall be unlawful for any person engaged in commerce, in the course of such commerce, knowingly to induce or receive a discrimination in price which is prohibited by this section."

While the buyer's liability for inducing or receiving a discriminatory promotional allowance is not set out in the Robinson-Patman Act, the Federal Trade Commission in the United States has proceeded against buyers under section 5 of the Federal Trade Commission Act which generally prohibits unfair methods of competition in commerce. Courts reviewing these prosecutions have upheld the Commissions' decisions in this regard (most notably, Fred Meyer Inc. v. F.T.C., 359 F. 2d. 351 (9th) Cir., (1966), rev'd on other grounds, 390 U.S. 341 (1968)).

Thus, the buyer's liability for price discrimination in the United States is explicit while in Canada buyer liability for the same offences is implicit, depending as it does on the interpretation of the Director of Investigation and Research as to certain words in section 34(1)(a).

The institution of buyer liability is consistent with the intention of both Acts to curb the buying advantages of the major retail grocery chains. In meeting this intention, however, the Robinson-Patman Act exposes the buyer to liability for hard bargaining over price. The United States Supreme Court has limited this exposure somewhat by holding, in a recent case involving the food retailer A&P, that buyer liability is derivative upon the seller's liability.* Thus, the buyer in that case was able to obtain a much lower price than its competitors because the seller could have established a meeting-competition defence to a charge of price discrimination. According to one commentator, the meaning of this case may be that the Court believes the freedom of buyers to bargain over price predominates over the need to prevent predatory price cutting and undue pressure on sellers by a powerful buyer.†

2. Enforcement of the Robinson-Patman Act

Section 2 of the Robinson-Patman Act may serve as the basis for a civil proceeding by three different parties: 1) the Federal Trade Commission, 2) the Department of Justice, and 3) a private plaintiff. Under existing liaison agreements between the Department of Justice and the Federal Trade Commission, the F.T.C. has taken primary responsibility for public enforcement of section 2 of the Robinson-Patman Act, leaving the Department of Justice with responsibility for criminal prosecutions under another

* Great Atlantic & Pacific Tea Co. Inc. v. F.T.C., 99 S. Ct. 925 (1979).

† Donald I. Baker, Nineteenth Annual Advanced Anti-Trust Seminar: Price Discrimination, (1979) p. 199.

section of the Act. Therefore, this section will discuss only the Federal Trade Commission's enforcement and the private damage action.

i) Private Enforcement

The private damage action has been the primary tool of Robinson-Patman Act enforcement, especially in the past fifteen to twenty years. Perhaps one reason for its popularity is that a plaintiff proving injury due to a violation of the Act or any anti-trust law is entitled to three times the amount of the actual damages, plus attorney's fees. This can be compared with the situation in Canada where, under section 31.1 of the Combines Investigation Act, a successful plaintiff may recover only the amount of damage proved to have been suffered, together with the cost of investigation.

It is also possible for a party to a legal action to engage an attorney on a contingent-fee basis in the United States. An attorney hired on a contingency basis is only paid if the action is successful in which case the attorney is paid from the damages. It is not proper to hire a lawyer on such a basis in Ontario.

ii) The Federal Trade Commission

The F.T.C. is an independent administrative agency, chartered by the United States Congress in 1914, that enforces U.S. anti-trust and consumer protection laws. In fact, it shares anti-trust jurisdiction with the Department

of Justice's Anti-Trust Division. However, an agreement between the two agencies prevents duplication of anti-trust effort. Roughly stated, the F.T.C. fulfills the functions given to both the Director of Investigation and Research and the Restrictive Trade Practices Commission by our Combines Investigation Act, and in fact, the F.T.C. has more enforcement power than both.

Like our agencies, the American agency has no power to levy fines. The F.T.C. does have power, however, to issue an order to cease and desist from violations of the Robinson-Patman Act. If a final litigated order of the F.T.C. were to be violated by someone ordered to cease and desist, the F.T.C. has the power to seek civil penalties for the violation of that order in a federal district court.

Under our system, neither the Director of Investigation and Research nor the Restrictive Trade Practices Commission has enforcement power. Their duties are to remit the matter for the ultimate consideration and decision of the Attorney-General. While our R.T.P.C. has power to issue cease and desist orders in relation to other matters, such power does not apply to discrimination under section 34 or 35. These sections are of a quasi-criminal nature and accordingly, the remedies for their infraction must be obtained in the courts.

The statutory mandate of the F.T.C. requires it to proceed only where the public interest is involved, although it is open to a private party to sue in any case.

The F.T.C. staff thus weighs very carefully the cases which are brought before it in an attempt to isolate the largest and most substantial violations involving firms gradually making the transition from competitor to monopolist.

The cost of prosecuting a case is substantial. In the A & P Case previously mentioned, the United States Commission expended 38,000 man-hours in a prosecution that was ultimately lost before the Supreme Court. The action consumed 110 days in hearings before the court of first instance alone. The length of proceedings may often be attributed to dilatory tactics on the part of the defence attorneys in an F.T.C. action. In one case (Herbert R. Gibson, Inc., et al, ALJ decision: March 22, 1979) approximately 150 motions were filed on behalf of the defence resulting in a cost of more than 27,000 hours of F.T.C. attorney time. In another case, the United States Commission expended more than 46,000 hours for a case (F.T.C. v. General Foods, decision as yet unreported) which had been before the courts for only two days and which would probably take a period of two years to complete. It was estimated that these man-hours can be multiplied by 30 to determine the approximate number of U.S. taxpayers' dollars spent on those cases.

It is this high, if not prohibitive, cost of enforcement coupled with the Commission's focus on substantial violations that has, no doubt, played no small part in the decrease in the number of formal investigations conducted by the agency from 159 in 1968, to 8 in 1979. Another factor leading to the shift in resource allocation away

from Robinson-Patman may be the increasing criticism to which the Act has been subjected. It is to this criticism that I now turn.

3. A Critical View of the Robinson-Patman Act

Those in favour of the Robinson-Patman Act are of the opinion that the legislation accomplishes its purpose in preventing price discrimination to the benefit of competition generally. In the absence of Robinson-Patman, the large and vertically integrated buyer would have *carte blanche* in dictating terms to its suppliers, proponents claim. Because of Robinson-Patman, the price reduction such a buyer can command is limited to the savings that can be proved.

Although it cannot be quantitatively demonstrated, there is no doubt that the large firm, carefully advised by counsel who are conscious of the expense and adverse publicity which a Robinson-Patman prosecution might generate, hesitates before revising downward price structures in favour of large buyers. There is also little doubt that the large firm consciously broadens the availability of promotional allowances and services in light of the Act's requirements in this regard.

Opponents* of the Act have questioned whether these effects are really virtues of the Act. They question the

* Opposition to the Robinson-Patman Act is perhaps best set out in United States Department of Justice, Report on the Robinson-Patman Act (Washington: 1976). Much of the material on this Act in this section of my Report is taken from this source.

desirability of legislation which, in an inflationary age, may militate against a reduction of prices. As we have seen, suppliers are presumed guilty if they give price differentials sufficient to affect retail prices, a presumption that is difficult to rebut. Buyers who try to negotiate the best possible price may similarly run afoul of Section 2(f). It is argued most persuasively that Robinson-Patman thus creates in the business community an atmosphere where caution, not competition, is the rule.

Opponents of Robinson-Patman also question the desirability of an Act whose primary purpose is to protect one sector of the economy, small business, from another sector. They claim that this purpose contradicts the aim of other U.S. anti-trust laws which is to promote and preserve competition as a whole.

It is further argued that Robinson-Patman indirectly raises price levels because business must pay dearly to comply with Robinson-Patman. The cost of compliance falls proportionately more heavily upon businesses with less financial resources.

The Act is also criticized by economists for suppressing a device whereby oligopolistic sellers engage in price competition. When selling to oligopolistic buyers, oligopolistic sellers will frequently grant special price concessions from announced price lists. Such price concessions may lead to the breakdown of collusive arrangements between sellers in an industry. By making such concessions illegal, Robinson-Patman may be suppressing one of the only

ways that prices can be reduced in an oligopolistic industry.

Opponents of Robinson-Patman also argue that the Act has led corporations to try evasive and often inefficient techniques in an attempt to avoid the consequences of the Act. Large grocery chains, for example, not only have integrated wholesaling functions but also acquire their own bakeries, dairies, coffee-processing and packing plants. They might develop their own "private" or "house" brands. Either of these methods not only remove these chains from the scope of the Act, but also take their business away from suppliers.

As for the small buyers, as we have seen, an association with a buying group may lead to prosecution if the buying group merely consolidates orders and does not accept delivery. This restricts the ability of independent retailers and wholesalers to obtain the same rebate as their larger competitors.

It is difficult to quantitatively analyze these criticisms. It cannot be said just how much or to what degree Robinson-Patman has had a detrimental or beneficial effect on competition in the United States.

We do know that the market structure of the retail trade in the United States substantially resembles that in Canada. When comparing the effects of federal legislation, it is appropriate to compare nationally based figures to minimize local, state or provincial effects. The United

States Census of Retail Trade indicates that over the entire United States in 1977, 59.7% of grocery stores sales (including combination stores) were accounted for by firms with eleven or more stores, which is the American definition of chain store. Using the Canadian definition of a chain as four or more stores, the same source of data indicates that these stores achieved 66.3% of United States grocery store sales in 1977. The Canadian chains (with four or more stores), as reported in Canadian Grocer Magazine, accounted for 59.8% of grocery and combination food store sales in 1977. Thus, it is possible to conclude that the differences in federal legislation by themselves do not produce a marked effect on the retail grocery market structure.

In summary, from what evidence is available, it is difficult to say that the Robinson-Patman Act has had any more effect on the growth of big buyers than comparable sections of the Combines Investigation Act have had. To the contrary, large retail firms seem to be thriving in the United States, probably for the reason that the advantages of large-scale operations outweigh any advantages that discriminatory pricing may give.

For these reasons, the Commission does not recommend enactment of legislation following the model of the United States' Robinson-Patman Act. It appears to be a costly cure with limited proven effectiveness and with potentially dangerous side effects.

C. Proposed Legislation for Ontario:

Bill C-13

The Ontario Federation of Agriculture Proposals

The Ontario Liberal Party Proposal

In the first section of this chapter, I examined the present legislation governing discounts, allowance and rebates in Canada. I found that the sections in the Combines Investigation Act affecting price discrimination have serious shortcomings which could hinder enforcement. I also found that the number of complaints raised under the sections is minimal.

In the second section of this chapter, I considered present legislation in the United States dealing with price discrimination. I found that the Robinson-Patman Act requires business in that country to comply with a stricter standard than the Combines Investigation Act. Nevertheless, it is not evident that this stricter standard has created a more competitive atmosphere in the United States, and, on the contrary, there is well-reasoned criticism suggesting that Robinson-Patman is in fact detrimental to the interests of consumers and even of small business.

In this section I turn to proposals for reform of our legislation. I will consider Bill C-13, a proposed amendment to the Combines Investigation Act brought before the federal parliament. The proposals I will consider in detail are proposals brought before this Commission by the

Ontario Federation of Agriculture and the Ontario Liberal Party which I was urged to adopt as my own in the form of a recommendation to the Government of Ontario.

By way of background to these proposals, I am obliged to indicate that representatives of the food industry who testified before the Commission were almost unanimously opposed to more legislation or regulation of any kind. Opponents to legislation include the most outspoken critics of the present state of competition. Opponents also included representatives from smaller businesses which, quite possibly, would have the most to gain from legislation restricting discounting practices.

1. Bill C-13

From time to time, draft legislation amending the *Combines Investigation Act* has been proposed to the federal government. The most significant of these proposals in relation to discounting practices is the amendment to the *Combines Investigation Act* proposed in Bill C-13 which was introduced in Parliament but not enacted at the close of the session in 1978. The text of the bill's sections relevant to this discussion are repeated in Appendix 9.

Bill C-13 proposed, in the words of the Director of Investigation and Research, a "half-way house" between the cost-justification requirement embodied in the *Robinson-Patman Act* and the absence of such a requirement. This bill would have retained the criminal offences in sections

34 and 35 with minor changes in wording to enlarge their scope.

The major change advanced by Bill C-13 is found in section 31.77. Section 31.77 would have allowed a new administrative agency to review price differences to competing customers where the supplier was a major supplier in a market or was one of the suppliers in a market where the practice was wide spread and where the practice impeded or was likely to impede the expansion of an efficient firm or a firm that would have been a strong competitor but for the practice. However, the board would not have been entitled to make an order where the supplier based the price differences on a reasonable assessment of the difference in actual or anticipated cost of supplying customers in different quantities and under different terms and conditions of delivery.

This proposal has two virtues, in my opinion.

The first virtue is that it is a proposal addressed to the federal government which, in my view, is the appropriate government to be dealing with this issue. I say this not only because our highest courts have upheld the Combines Investigation Act as a valid exercise of federal legislation several times, but also because there are sound practical reasons for Ontario to cede this authority to the federal government. Economic activity today ignores provincial boundaries. Labour, capital, and technology are highly mobile. The market for fruit and vegetables, for

instance, is often a national and even international market as shown in Chapter 4. It makes sense to vest the authority to prosecute unlawful transactions, often involving national and multi-national companies who deal with each other on a country-wide basis, in the federal government which has the means and resources to combat these practices.

The second virtue relates to the first in that the draft section 31.77 would have required the showing of an adverse effect on competition, an effect not now required by section 34(1)(a) or section 35. This sort of evaluation of evidence is one that requires a great deal of expertise on the part of the evaluator. This confirms my opinion that such decisions should be made at the federal level where this expertise now resides.

With these comments in mind, I now turn to the proposals recommended for Ontario tabled before this Commission.

2. The Ontario Federation of Agriculture Proposal

In its final brief to the Commission, the Ontario Federation of Agriculture (O.F.A.) submitted draft legislation which it proposed that the Ontario government enact in regard to various areas.

i) Draft Price Discrimination Legislation

The O.F.A. submitted that Ontario needs price discrimination legislation to deal with the Federation's

perception that, "there is price discrimination in the existing discount system and thus it represents unfair competition." It urged that the Government of Ontario provide legislation to "parallel the development in the United States, where increasing action at the state level to protect against price discrimination is encouraged as complementary" to federal enforcement.

This Commission has not found that the existing discount system is inherently discriminatory, nor has it found that the system represents unfair competition. In regard to the United States' statutes against price discrimination at the state level, it should be noted that this is a necessity having regard to the different constitutional division of powers in that country. The Robinson-Patman Act cannot apply to most intra-state transactions because of the jurisdictional requirements of that Act and because of the United States Constitution which limits application of federal legislation to interstate commerce. The same limitation does not apply to the Combines Investigation Act which is, as discussed, criminal law. In Canada, criminal law is a matter for federal legislation no matter whether the transaction occurred entirely inside or outside the province.

Furthermore, the enactment of provincial price-discrimination legislation would raise serious questions as to its enforceability vis à vis nearly one-half the value of food products sold by Ontario supermarkets and consumed by Ontarians, the one-half being the approximate proportion of produce originating from outside the province. Depending

on what effect price-discrimination legislation would have on the price of food commodities, such legislation could have serious consequences for the competitive position of Ontario-grown produce.

ii) Recommended Ban on Discounts to Farmers and Grower-Packers

The O.F.A. also submitted a recommendation that the Ontario Government prohibit all discounts or other reductions in price to farmers, growers and grower/packers. I am of the opinion that this is too sweeping a prohibition. It is a prohibition that fails to account for discounts and other reductions in price to which farmers, growers and grower/packers willingly consent.

There are examples of such discounting in the various marketing board agreements. For example, the agreement for marketing the 1979 crop of lima beans for processing, an agreement sanctioned by the Farm Products Marketing Board, provides that the processor may deduct from the purchase price a certain sum for services of harvesting and transporting lima beans in sections 8 and 9 of the agreement. This is one example of a reduction in price which could be swept into the net of prohibited reductions.

iii) Recommended Legislation Respecting Mergers

The O.F.A. also proposed legislation to deal with vertical and horizontal integration. It was suggested that

the Business Practices Division of the Ontario Ministry of Consumer and Commercial Relations should have the power to prohibit and disallow those mergers which would damage competition. This Commission is of the view that such a recommendation is beyond the powers expressed in its terms of reference.

I note, however, that such legislation would give a government body enormous power of interference in the affairs of private companies engaged in a free market economy. I am not saying that such interference is never warranted. However, I question the wisdom of giving such power to a provincial administrative body when this power presently resides in competent federal authorities. I also note that the same power can be stimulated into action by the formal or informal complaints of Ontario residents pursuant to the provisions of the Combines Investigation Act.

iv) Recommended Legislation Respecting Private Label Merchandise

The O.F.A. also proposed legislation to require that all packaged and labelled grocery goods should carry on the label the name and location of the manufacturer or packer. Again, I believe such a recommendation to be beyond my terms of reference. I have heard no evidence to suggest that such legislation would have any effect on discounting practices.

v) Recommended Policy Respecting Economic Development Planning

The O.F.A. finally recommended a policy position for the Ontario Government in dealing with the issue of economic and development planning generally, and with shopping centre locations in particular.

In effect, it is recommended that policies be reviewed with regard to their effects on small- and medium-sized business, especially as to providing opportunities for independent retailers to secure locations in shopping centres and other key commercial growth areas.

This recommendation is expressed in such general terms that I doubt it will provide much direction for those charged with planning the affairs of this province. Furthermore, I would hesitate to recommend to the government that it consider protection of any class of business in preference to any other class when deciding matters of policy. It is the welfare of the people of Ontario as a whole -- as businessmen, as food producers, as consumers -- which concerns the government.

Having said this, I am quite certain that the progress and growth of independent retailers and other small- and medium-sized business does concern the government in policy formulation. The one example provided to me as to possible discrimination concerned an independent retailer's site location in the town of Tillsonburg. I am told this

situation resolved itself in favour of that retailer. Considering this case and the publicity that surrounded it, I am certain that the government is now conscious, if it was not before, of this issue in economic planning.

3. The Ontario Liberal Party Proposal

In his appearance before the Commission, Dr. Stuart Smith, leader of the Ontario Liberal Party, presented draft legislation which he requested that I consider and recommend to the Ontario Government. This draft appeared in substantially the same form as part of a Private Member Bill submitted under the name of Mr. Jack Riddell, Liberal Member of Parliament, to be introduced before Parliament as Bill Number 208. Bill 208 died on the order paper at the end of the 1979 session and has been reintroduced as Bill 23 in the 1980 session. The texts of the draft presented before me and of the Private Member Bill presented to the legislature are included in Appendix 9.

Dr. Smith submitted that discounting, as presently practiced, may lead to adverse long-term economic effects in that such practices drive small food retailers out of business. This enables a few very large firms to dominate the market; hence, the need for legislation.

With all due respect to Dr. Smith, this Commission has not found evidence in this Inquiry to support his conclusion. The isolated and minor incidents raised before me -- for example, the Shebec incident detailed in Chapter 3 --

could have been avoided with more prior consultation on the part of both buyer and seller. For this reason, I am adverse to recommending the sledge-hammer approach of this legislation and I prefer, instead, an approach combining mediation and co-operation (see Chapter 18 for my recommendation).

This is not to say that discounting is never or could never be a problem. On the contrary, it could cause difficulty in the economy if larger firms extracted price concessions so as to obtain market dominance over smaller competitors. However, this Commission has not found this to be the case in Ontario at the present time. Moreover, discounting of this magnitude, I believe, should be controlled by the federal government for the reasons mentioned earlier in this section. That is, the federal government is in a better position from the standpoint both of expertise and of jurisdiction, to deal with companies and transactions which transcend provincial and national boundaries.

In fairness to Dr. Smith, his presentation does consider the federal legislation and its constitutionality. I agree that the Act's criminal-law basis is a source of difficulty for its enforcement. Since penal consequences are involved, the standard of proof required is perhaps a higher standard than economic considerations and circumstances would warrant.

Dr. Smith proposes that these constitutional difficulties can be overcome by constituting such legislation as an

amendment to the Ontario Farm Products Marketing Act. Because the Farm Products Marketing Act has been upheld by the courts as constitutionally valid provincial legislation on the basis of provincial jurisdiction over agriculture, Dr. Smith argues that such an amendment would be valid.

I question the constitutional and practical feasibility of this suggestion. According to the "pith and substance" doctrine developed by the courts in relation to interpretation of the British North America Act, the courts must determine the pith and substance of such an amendment. Arguably, in this case, the pith and substance of this proposed amendment does not relate to agriculture, but rather relates to competition policy. It is generally accepted that the power to regulate competition policy resides in the federal government.

Dr. Smith's draft legislation would give the Farm Products Marketing Board jurisdiction to order compliance with the prohibitions stated in the legislation. I question the Farm Products Marketing Board's ability to deal with competition problems in as competent a manner as the Director of Investigation and Research and his staff.

For all of these reasons, I am unable to recommend the proposals submitted by the Ontario Liberal party.

D. Conclusions

The following is a summary of my conclusions on the evidence examined in this chapter:

1. The Combines Investigation Act does have shortcomings which prevent it from being as effective as it might be. I do not, however, subscribe to the opinion of some, expressed before me, that this legislation is vacuous and ineffective. On the contrary, there is evidence that the companies involved are quite aware of this legislation and endeavour to comply with it.

2. The Robinson-Patman Act, legislation controlling discounting in the United States, has serious defects which prevent it from being a suitable legislative model for this country. In addition, the testimony I have heard from all levels of the food industry was almost unanimous to the effect that more legislation is not desirable or advisable at the present time. Such comments were made not only by representatives of the larger firms, but also by representatives from that class of business which these proposals purportedly would protect: small- and medium-sized business.

3. In respect of the United States legislation, the Robinson-Patman Act, I have considered and rejected the importation into Canada of the stricter standard of liability which this legislation

imposes. Even if I were convinced that small business needs a stricter standard to protect it from larger competitors, I am not convinced that the Robinson-Patman Act accomplishes this purpose. Indeed, I question whether this statute does not unduly restrict the affairs of business in the United States and in so doing, result in higher prices for food products to the detriment of consumers.

4. In respect of the proposals submitted by the Ontario Federation of Agriculture and the Ontario Liberal Party, I would first like to express my appreciation to both these organizations for the effort and care put into advancing these proposals. On the other hand, I cannot recommend either of these proposals to the Ontario government. On the basis of the evidence submitted to this Commission, I do not find that the magnitude of the problem indicated by the evidence warrants the solutions proposed.

5. If this problem were in the future to become as grave as these two organizations believe it will, then the proper body to pass such legislation would be the Government of Canada and not the Government of Ontario. This is so because the problem they perceive is a problem of competition policy requiring an approach that integrates legislation related to discounts and legislation related to other aspects of competition as well.

For example, I think it is quite possible that a retailer restricted as to its bargaining with suppliers would consider alternative means, such as vertical integration, of achieving the same ends. I do not think the Ontario Government has the jurisdiction or the effective means to apply and enforce the sanctions necessary to preserve competition in an economy where companies transacting business on a national and international basis are the rule rather than the exception.

6. In order to meet the particular problems disclosed by the evidence in this inquiry, I recommend that the Ontario Government follow the path of arbitration rather than of legislation. My recommendation in this regard is expressed in Chapter 18.

CHAPTER 17

FINDINGS OF OTHER INQUIRIES AND STUDIES

FINDINGS OF OTHER INQUIRIES AND STUDIES

GENERAL

It can be stated, with a reasonable degree of assurance, that no other segment of the Canadian economy has been so closely scrutinized as the food industry in the past 20 years. There have been numerous Royal Commissions, studies and inquiries into various aspects of the industry. In 1977, the Department of Consumer and Corporate Affairs published a bibliography entitled A Review of Research on the Canadian Food Industry. It listed over 900 studies of Canada's food system.

During this Inquiry, the Commission has been referred to several studies, reports and other documents. In addition, the Inquiry staff researched many relevant sources on its own. Appendix 10 lists some of the reference material studied by the Inquiry staff.

In the following pages of this Chapter, I have summarized the findings of several reports which deal with the issue of rebates directly or in relation to corporate concentration and market power.

REBATES AND ALLOWANCES IN THE BRITISH COLUMBIA FOOD INDUSTRY, 1978

This Report* is one of a series resulting from a research programme undertaken for the British Columbia Legislature by its Select Committee on Agriculture. The series reviews the entire food industry in British Columbia.

The objectives of this particular report are:

(1) to gather information about rebates in British Columbia, and in particular to determine the total volume of payments involved;

(2) to determine their impact on the British Columbia food industry;

(3) to clarify some of the misunderstandings that appear to exist about this subject.

The significant difference between the British Columbia Inquiry and the present Inquiry is that the B.C. Inquiry was <u>not</u> required to consider the effects of rebating on the price levels to farmers and consumers. This is the major term of reference for my Inquiry.

Information for the British Columbia study was obtained from public hearings, questionnaires, and interviews with representatives of processing companies, and

* British Columbia Select Standing Committee on Agriculture, <u>Rebates and Allowances in the British Columbia Food Industry</u> (June, 1978).

wholesalers, brokerage and distributing firms and retailers operating in British Columbia. This Inquiry followed a similar procedure, but was more concerned with operations in Ontario, of course.

The Committee made the following findings, among others:

(1) That total rebates received by buyers of food products amounted to approximately 2.2% of the total retail sales. The Committee acknowledged that this figure could be higher for larger buyers due to sliding-scale calculations.

In Chapter 9 of this Report, I concluded that retailers receive rebates by cheque in the amount of 2.48% of sales. In addition, I concluded that they receive off-invoice allowances estimated at 3.5% for the large retailers. It would appear from reading the British Columbia Report that the Committee did not estimate the off-invoice allowances, perhaps because of the different accounting treatment for these rebates mentioned in Chapter 9.

(2) That there was no evidence of delisting by retailers due to a supplier's failure to offer acceptable rebates or refusal to engage in promotional programs.

This finding corresponds with my own, as detailed in Chapter 15.

(3) That there was no evidence that rebates added to the cost of food although there was evidence that they assisted in lowering food prices when passed through to consumers.

This finding also corresponds with my own, as detailed in Chapter 9.

(4) That rebating practices are seriously misunderstood, not only by consumers but also by those in the food industry.

(5) That previous public inquiries investigating the food industry have only superficially analyzed rebates. Such superficial analyses have only contributed to the confusion about the subject. The Report accordingly advised against undertaking further inquiries into the practice.

The study concluded that the resolution of any of the problems which arise from rebates is difficult. It depends to a large degree on what type and size of enterprise is desirable at the various levels of the food chain: large or small retailers or wholesalers, corporate chains or independents, vertically integrated or not, and so on.

INQUIRY ON WHOLESALE AND RETAIL PRICING PRACTICES FOR FLUID MILK IN ONTARIO, 1977

The Milk Commission of Ontario conducted this intensive Inquiry.* The Inquiry was instituted mainly due to the substantial increase in the price of fluid milk in 1973 and 1974, an increase that was alleged to be not justified.

The Milk Commission determined that nearly all retailers, including independents except for the very small, received rebates. Discount levels in 1975 ranged from 15% to 24%, depending on sales volume and discounting methods. Whether or not these rebates were passed through to consumers depended on the competition in the particular retail market.

The Commission considered and rejected price controls as a solution to volume discounting. To enforce controls would be costly, they pointed out, and of doubtful efficacy. Referring to research in the United States on the subject, the Commission found that markets with controls were characterized by higher gross margins and higher profits than markets which were more freely competitive.

The Milk Commission concluded that the marketing system for fluid milk in Ontario, in which rebates play an integral part, was relatively efficient, progressive, flexible and equitable.

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* Inquiry on Wholesale and Retail Pricing Practices for Fluid Milk in Ontario, 1971 to 1975, Report, Milk Commission of Ontario, Toronto, 1977.

This paper* by Professor Bruce Mallen was commissioned by the federal Food Prices Review Board. The mandate of the Board was terminated before the paper was completed. Consequently, the paper expresses the view of the author and not necessarily the view of the Board.

The author found that the Canadian retail food trade is highly concentrated in urban areas. One negative consequence of high concentration is high prices, Mallen concluded. However, it is not discounting but rather barriers to shopping centre sites and economies of local advertising that are the basic determinants of concentration, the Mallen Report found.

The report considered eliminating or severely restricting the amount of volume discounts and promotional allowances but rejected these options. The author concluded that to the extent that rebates reflect real cost savings to suppliers, to disallow them would mean higher prices to consumers. By permitting rebates, there is at least the opportunity for retailers to pass savings through to consumers. In Professor Mallen's words: "Finally, there is no strong evidence that such discounts and allowances have been major contributors to concentration."†

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* Food Prices Review Board, Reference Paper No. 6, _A Preliminary Paper on the Levels, Causes and Effects of Economic Concentration in the Canadian Retail Food Trade: A Study of Supermarket Power_, (Montreal; 1976).

† _Ibid_, p. 162.

RETAIL OLIGOPOLY - AN EMPIRICAL STUDY OF THE GROCERY TRADE ON THE PRAIRIES, 1968

This study* was conducted by Professor Peter C. Dooley for the Prarie Provinces' Royal Commission on Consumer Problems and Inflation.† Professor Dooley analyzed the issues of corporate concentration, product differentiation, demand, costs, and barriers to entry and exit from the grocery trade.

Professor Dooley concluded that rebates give to chain stores and to large independent retailers cost advantages over their smaller competitors. He found no evidence that rebates were cost justified. To properly analyze this issue, one would need a more detailed investigation of manufacturing, transportation and warehouse costs, Professor Dooley explained.

Professor Dooley did not consider the situation in Ontario where small retailers are likely to purchase from wholesalers and through buying groups which receive substantial rebates.

* Royal Commission on Consumer Problems and Inflation, Supporting Study No. 3, Retail Oligopoly: An Empirical Study of the Structure, Conduct and Performance of the Grocery Trade on the Prairies, by Peter Dooley, (Regina: 1968.)

† Also known as The Prairie Provinces Cost Study Commission, and, by its Commissioner's name, as the Batten Report.

REPORT OF THE ROYAL COMMISSION ON PRICE SPREADS OF FOOD PRODUCTS, 1959*

This Federal Royal Commission inquired into the extent and causes of the spread between the prices received by producers and the prices paid by consumers for farm and fisheries products between the years 1947 and 1958.

The Commission found that processors and producers were declining in number and were selling their products to fewer and more powerful buyers. As a result of competitive pressure, processors offered a system of discounts and allowances.

The Commission also found a tendency towards service competition rather than price competition in the industry which results in more advertising and promotional activities as opposed to lower prices for the product. The Commission found that promotional activity is closely related to the system of discounts and allowances as the processors often pay for such services by offering lower prices to the retailers.

The report did not indicate what savings a supplier might obtain in promoting products through retailers who receive advertising rebates from the media. The report also neglected to mention the benefits of point-of-sale promotion paid for by advertising allowances.

* Royal Commission on Price Spreads of Food Products, Report, (Ottawa, 1959).

REPORT ON DISCRIMINATORY PRACTICES IN THE GROCERY TRADE, 1958

This study* was conducted by Dr. Lawrence A. Skeoch as part of a report of the federal Restrictive Trade Practices Commission, a federal office appointed pursuant to the *Combines Investigation Act*. The purpose of the study was to examine complaints of price discrimination through rebates, the allegation being that such rebates were prompted by competitive pressure rather than by cost savings.

From a survey of food suppliers, Dr. Skeoch found that there were substantial differences in the rates of special rebates among the categories of grocery buyers. Certain buyers received favoured treatment from suppliers, especially in respect of advertising allowances.

Dr. Skeoch suggested that suppliers review the desirability of discounting as opposed to a system of reducing list prices to buyers, reductions that may be passed on to the consumer in the form of lower consumer prices.

Parliament reacted to the report of Dr. Skeoch, and to the report of the 1959 Royal Commission that followed, by passing what presently exists as section 35 of *The Combines Investigation Act*. This section provides for proportionality with respect to price concessions granted for advertising or display purposes.

* Restrictive Trade Practices Commission, *Report Transmitting a Study of Certain Discriminatory Pricing Practices in the Grocery Trade made by the Director of Investigation and Research*, (Ottawa: 1958).

CONCLUSIONS

The following summarizes my conclusions on the material examined in this chapter:

1. To a degree, it is beneficial to consider the conclusions arrived at by previous studies and inquiries. However, such conclusions are not always applicable to the present context due to differences in industry structures and marketing patterns which vary with time and market area.

2. I agree with the 1978 report of the British Columbia Select Committee that most previous investigations, but not all, have treated the subject of rebates in a superficial manner and have only added to the confusion surrounding this subject. I also concur with the recommendation in that report that no further studies of the food industry are necessary or desirable at the present time.

3. I agree with the findings of the 1977 Report of the Milk Commission of Ontario that the marketing system for fluid milk in Ontario, a system in which rebates play an important role, is relatively efficient and equitable.

4. I agree with the Mallen Report's conclusion that there is no strong evidence that rebates have been a major contribution to concentration. I am

unable to agree with Professor Mallen that concentration in Canadian food retail markets leads to prices higher than they should be, particularly in Ontario. However, in fairness to Professor Mallen, I must say that I have not studied this question in the depth that he has studied it, nor do my terms of reference permit me to do so.

CHAPTER 18

OVERVIEW OF THE FOOD INDUSTRY

OVERVIEW OF THE FOOD INDUSTRY

GENERAL

During the course of the Inquiry, a great deal of evidence was heard that was not specifically relevant to the terms of reference. Nevertheless, I admitted this evidence because it enabled the Commission to consider rebates in the perspective of the food industry as a whole. I think it would be remiss on my part if I did not report, in a general way, my impressions of the food industry in Ontario, deduced from this evidence.

IMPORTANCE OF THE FOOD INDUSTRY

The food industry is vital to the residents of Ontario. We depend to a large extent on the food chain of Ontario -- producer, processor, wholesaler and retailer -- to deliver our nutrition. The citizens expect a large variety of good quality food at a reasonable price.

Although statistics are not available, it is quite safe to state that more persons are engaged in the food industry than in any other industry in the province.

These basic facts underline the importance of this Inquiry. That is why the Inquiry investigated the food industry in such depth to determine if rebating has a negative effect on farmers and consumers.

Is the Ontario food industry efficient? To answer this question begs another. Can the residents of Ontario purchase a large variety of quality foods at reasonable prices?

The witnesses at the Inquiry answered this question almost unanimously in the affirmative. There is no question that the Ontario farmer produces high quality products. As a result of continuing research, the quality and variety are improving. The shelves of the retailers are stocked not only with Ontario food products but with products from all over the world.

The improvement in the marketing of food in the past twenty years has been almost revolutionary. New technology, such as scanning, is being developed and refined to further facilitate the purchase of food.

And now to the bottom line -- are food prices reasonable in Ontario? To answer this question, one must consider food prices in relation to disposable income.

A survey* conducted in 1979 found that on 21 food items, Canadians have the most reasonable food prices in the world, based on their take-home pay. The 21 items

* Jane K. Phillips, Foreign Agriculture magazine, (Foreign Agriculture Service, U.S. Department of Agriculture Feb. 5, 1979).

included such basic foods as meat, bread, rice, sugar, fresh fruits and vegetables. The survey was performed in sixteen world capitals.

The survey also disclosed that the average Canadian spent $13.30 on food for home consumption out of every $100 left in the pay cheque after taxes. Only Americans paid less -- $12.50 for every $100 in take-home pay.

The survey considered how many hours a person had to work to pay for the basket of food. It found that an average Ottawa resident worked 8 1/2 hours to pay for the basket while a resident of Washington D.C. worked ten minutes more, a resident of Tokyo 29 hours, and a resident of Brasilia 69 hours.

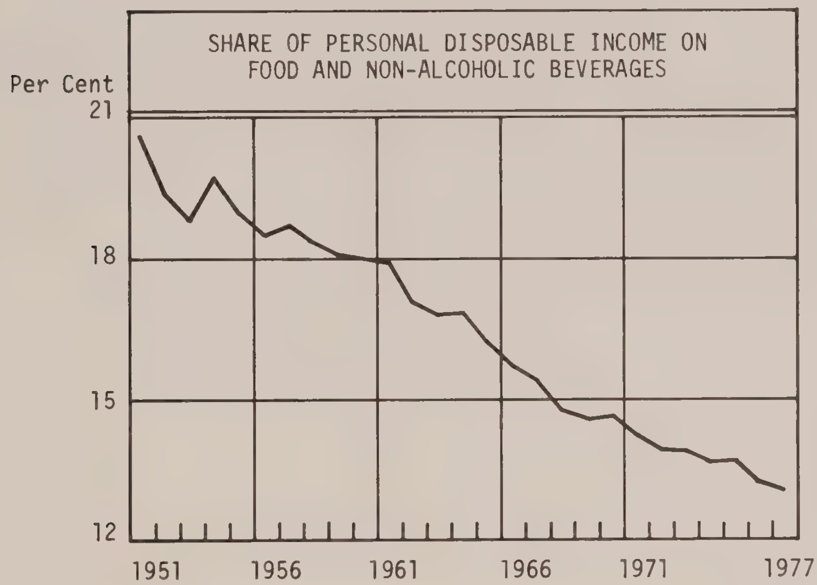
The G.P.M.C. indicated that, in 1949, the average Canadian expended 29% of take-home pay on food. By 1968 the percentage decreased to 15% and by 1977 to 13.1%. In 1978, this percentage increased only slightly to 13.2. These figures are illustrated in Figure 18-A.

In 1978, the Grocery Products Manufacturers of Canada had prepared for it a paper entitled Food Price Facts 1971-78. Included in this paper was Figure 18-B indicating the minutes worked to purchase a selection of food items 1960-78. Almost all items required less work-time in 1978 than in 1960.

FIGURE 18-A

SHARE OF PERSONAL DISPOSABLE INCOME

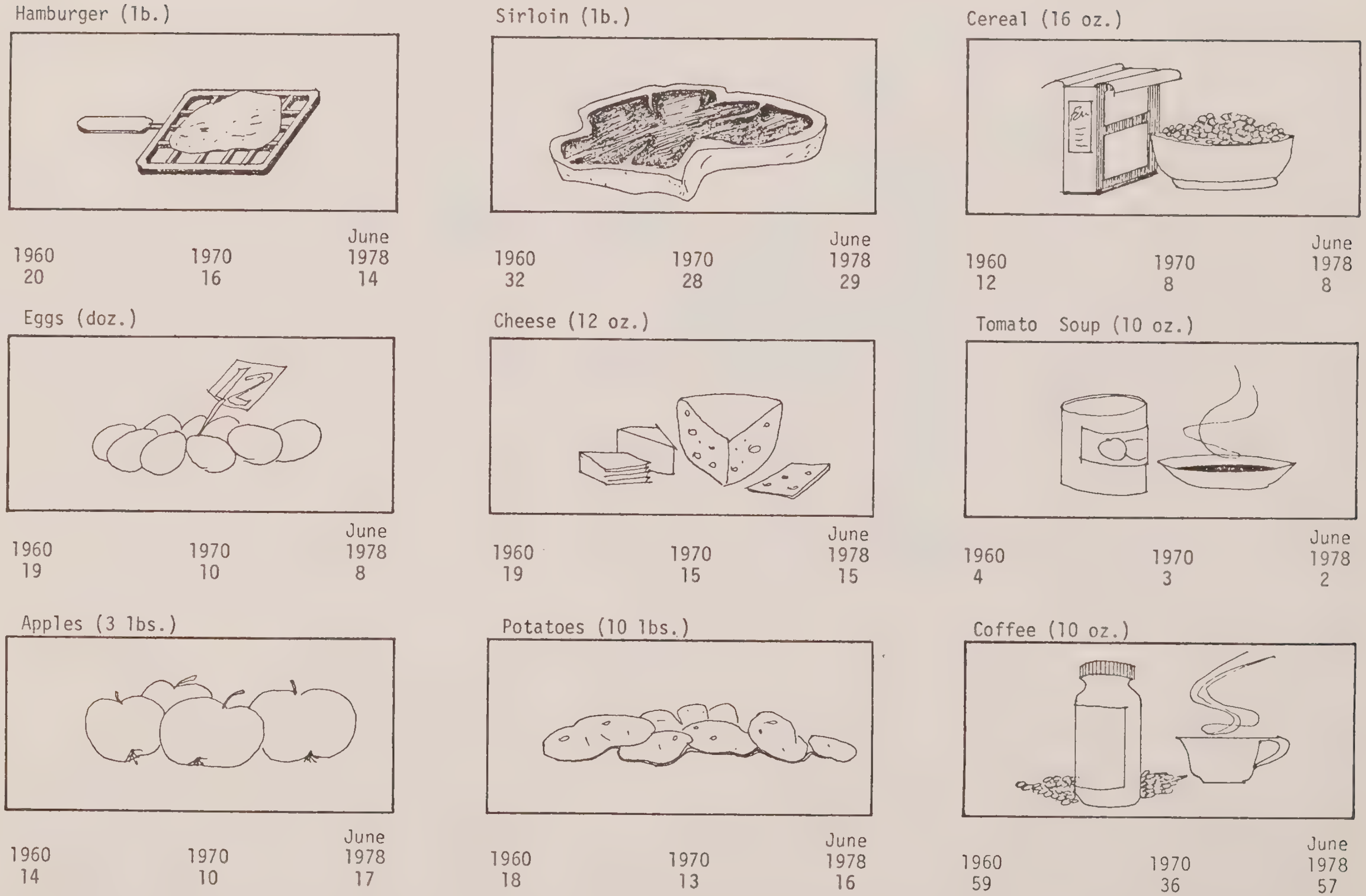
SPENT ON FOOD AND NON-ALCOHOLIC BEVERAGES, 1951 - 1977



SOURCE: Statistics Canada, National Income and Expenditure Accounts, Cat. No. 13.001. Submitted by G.P.M.C. in their Brief to the Commission.

FIGURE 18-B

MINUTES WORKED TO PURCHASE A SELECTION OF FOOD ITEMS
1960 - 1978



NOTE: Apple and potato figures are distorted because of seasonal variations.

SOURCE: Calculated from price data supplied by Charles Ambler & Associates Limited and Statistics Canada, Employment Earnings and Hours, Cat. No. 72-002. Submitted by G.P.M.C. in their Brief to the Commission.

In 1979 the Union Bank of Switzerland published a paper entitled <u>Prices and Earnings Around the Globe</u>.* This paper surveyed 45 major international cities in terms of the purchasing power that a selected group of wage and salary earners possess. Toronto ranks fifth among cities based on <u>net</u> purchasing power levels of a complete basket of goods and services. Toronto ties for tenth position when only food is considered.

In 1977 the federal Department of Consumer and Corporate Affairs published a paper entitled <u>A Review of Research on the Canadian Food Industry</u>. The reports reviewed indicate that the Ontario consumer is served by one of the most efficient food systems in the world.

My conclusion is that -- after considering the evidence at the Inquiry, and all surveys and reports referred to me -- Ontario is served by one of the most efficient food systems in the world. This is a remarkable achievement particularly in light of our low population density, long transportation distances and short growing season.

<u>NEGATIVE ASPECTS OF THE ONTARIO FOOD INDUSTRY</u>

One would think that the achievement of such an efficient food system must be the result of a spirit of co-operation between all levels. This is not always the case. Although the producer, processor, wholesaler and retailer all depend on each other for success in the food

* UBS Publications on Business, Banking and Monetary Problems, Vol. 69, Toronto, 1979.

industry, they appear to adopt an adversary position toward each other. All levels of the food industry are in business to make a profit and one can expect differences of opinion between buyers and sellers, but the evidence indicated the animosity extends beyond this point.

The Ontario Federation of Agriculture represented the agricultural community at the Inquiry. The Federation was highly critical of the supermarket chains. In the O.F.A.'s view, the chains dominate the market by their purchasing power. The Federation is not convinced that there is real competition in prices between the chains. It is also concerned about the large share of market held by Dominion Stores and Loblaws, submitting that these chains use their power to exact rebates from producers and food processors.

The Grocery Products Manufacturers of Canada similarly feels that suppliers may be intimidated by the chains and their market power.

Many small retailers are confused about rebates, and feel they are not sufficiently informed about them. They oppose the loss-leader selling by the chains.

Many of the large chains resent marketing boards and express the view that they cause an increase in the price of regulated farm products. For example, the president of one of the chains testified that eggs are over priced by 25 cents per dozen due to quota and price regulations.

The entire food industry is concerned about the numerous inquiries into the industry. One witness testified that politicians are continually looking for a villain. He suggested that twenty inquiries in the past twenty years have found no wrong-doing.

There is no question that inquiries increase the cost of food. All those represented at the Inquiry have to pass their counsel fees and inquiry costs through to the consumer. In addition, the cost of the Inquiry office and staff has to be paid from the provincial funds.

I am seriously concerned about the discord and confusion in the industry in connection with rebating practices. Unless some remedial action is taken, there could be serious consequences, not only for the industry but also for the consumer.

With respect, I would like to suggest certain action by the Legislature that hopefully would improve the situation for both the industry and the consumer.

RECOMMENDATION

At the present time, no forum exists where the various levels of the food industry can meet in a constructive manner to resolve problems arising in the industry.

A forum should be established to:

(a) receive and arbitrate complaints about rebating practices;

(b) bring producers, processors and retailers together to mediate problems that exist or arise;

(c) inform all levels of the industry as to discounting practices;

(d) foster a spirit of co-operation between all levels of the industry;

(e) formulate a code of ethics for the industry.

This Inquiry has not made a comprehensive study as to the constitution of such a forum. If the Legislature feels that such a forum would serve a beneficial purpose, I would undertake to perform such a study and report.

The Commission has made cursory inquiries in other jurisdictions to ascertain their solutions to problems in the food industry. The Commission visited the State of California and was impressed with the spirit of cooperation that existed between producers and retailers. The industry works together on quality control, product development and marketing. There is little serious government intervention.

The Report on Rebates and Allowances in the British Columbia Food Industry recommended that the B.C. Ministry of Consumer and Corporate Affairs or the Ministry of Agriculture act as receiver and arbitrator of complaints in the food industry.

Sweden has created an anti-trust ombudsman who resolves problems in the marketplace. The principle tools used are mediation and publicity.

It is significant, in my opinion, that the chains' discounting of certain farm produce was discontinued coincidentally with the events leading to the institution of this Inquiry.

Subject to further study, it is my view that the forum should be an ongoing body separate from government and any sector of the food industry. It should be chaired by an independent person, such as a judge, with a counsel and a small investigative staff all of whom would be hired on a part-time basis.

In my view, such a body would have a salutary effect upon the behaviour of different segments of the industry. The Commissioner would, in effect, be an ombudsman for the food industry.

The idea of an independent body monitoring the food industry in Ontario is not an entirely new one. Under the Ontario Food Council Act,* repealed in 1979, the Food Council had jurisdiction to receive complaints and collect data respecting trade practices in the food industry. The former Chairman of the Ontario Food Council, Mr. Douglas Williams, testified that the Council was primarily occupied with production and marketing processes and acted in the

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* The Ontario Producers, Processors, Distributors and Consumers Food Council Act, R.S.O. 1970, c. 238, s. 6(3).

area of trade practices only when specific complaints were received. The Council responded satisfactorily to these complaints, as I have discussed in Chapter 3, Effect of Rebates on Farmers. In those instances, the approach I am recommending seems to have met with some success.

Several witnesses, including the Retail Council of Canada, felt such a body could serve a useful purpose at minimal expense. It is my view that if such a body had existed at the time that complaints as to discounting practices arose, then this long and expensive Inquiry could have been avoided.

CONCLUSION

The following summarizes my conclusion on the material examined in this chapter:

1. There is an undue amount of animosity between the various levels of the food chain in Ontario. This antagonism could eventually be detrimental to what is now an extremely efficient and inexpensive food distribution system.

RECOMMENDATION

1. In order to deal with this animosity, I recommend that the Government of Ontario constitute a forum of arbitration and mediation separate and apart from both government and any particular sector of the food industry.

CHAPTER 19

COMPENDIUM OF CONCLUSIONS

COMPENDIUM OF CONCLUSIONS

This chapter is a collection of the conclusions and recommendations from each chapter of my Report.

CHAPTER 2 - THE ONTARIO FOOD CHAIN

1. The system of discounting presently existing in Ontario is a rational and regular method of marketing food products benefitting both processor and retailer. Its effect on the farmer and on the consumer will be considered in subsequent chapters.

2. Rebates are paid almost exclusively by sellers of processed and manufactured goods to wholesale and retail buyers.

3. There are twenty distinct types of rebates which can be categorized into five functionally distinct groups of rebates that are listed in order of importance: advertising, economies of scale, finance, service and miscellaneous.

4. Each group of rebates serves a general purpose in the processor/manufacturer's marketing program. Advertising rebates generally pay for co-operative efforts designed to promote food products. Economies-of-scale rebates generally recognize economies realized by volume sales of these products. Finance rebates generally invite terms of payment favourable to the

seller's finances. Service rebates generally encourage the buyer to provide services in connection with the sale and distribution of these products.

5. Rebate amounts differ depending on the product group. Rebate amounts paid on the sale of dairy goods are much higher than on the sale of any other product group. For this reason, dairy rebates are considered separately in Chapter 6, Milk Processors and Rebates.

6. In addition to rebates received in the form of payment by cheque, retailers receive rebates in the form of reductions from invoiced amounts called "off-invoice allowances." Off-invoice allowances are not generally recorded as separate items in accounting records and therefore must be estimated. All references to rebates in this report include off-invoice allowances, except where these allowances are specifically excluded.

CHAPTER 3 - EFFECT OF REBATES OF FARMERS

1. Farm products are subject to complex and varied systems of sale in Ontario.

2. The sale of 40 farm products representing 57% of the 1977 total receipts for Ontario farm products is regulated by 23 marketing boards. Producers under marketing boards experience no rebating without the knowledge and consent of their boards.

3. The sale of farm products representing 43% of 1977 total receipts is not subject to marketing board regulation. There was no evidence of, nor did investigations indicate, any systematic rebating in respect of livestock and field crops except for one incident reported to the Ontario Food Council in 1977. The only evidence of rebating pertains to non-regulated fresh vegetables and fruit as summarized in the next number.

4. From time to time prior to 1978, rebating has occurred in respect of fresh vegetables and fruit not regulated by marketing boards. The total sales of these products represent approximately 3.4% of the total receipts for Ontario farm produce. In respect of these practices, I have reached the following conclusions:

   (a) that the reasons for these rebates were not understood by the growers involved;

   (b) that the rebates were not illegal but were the result of hard bargaining;

   (c) that these practices were discontinued by 1979 as the result of the actions of the Ontario Food Council and the adverse publicity generated by the Resources Development Committee and this Royal Commission.

5. Certain producers of non-regulated fresh vegetables and fruits are in a very weak bargaining position. This is true of the producers of perishable products such as tomatoes, strawberries and cherries who must sell their produce within a short period of time or risk losing their investment.

RECOMMENDATION

1. It is unfair for a retailer to obtain non-negotiable rebates from producers of fresh vegetables and fruits whose products are perishable. Although systematic discounting does not appear to be practiced in respect of such commodities at the present time, it is my recommendation that the Legislature should provide for the creation of a "watchdog" mechanism to ensure that discounting practices do not reappear. Such a solution is necessary because of the intense competition between retail chains in Ontario to buy as cheaply as possible.

CHAPTER 4 - IMPORTS AND REBATES

1. Generally, imported agricultural products are not subject to rebates in Ontario. Imported products are usually bought on a net price basis.

2. The pricing structure applying to imports from the United States, Canada's largest trading partner, is strongly influenced if not controlled by legislation in that country pertaining to discounting. Because of this legislation and because of the international competitive structure, there is little likelihood of rebates becoming an important factor in the price determination of agricultural products imported into Ontario.

1. Processors are the principal source of rebates in the food industry.

2. Processors offer rebates to retailers and wholesalers in order to sell more products.

3. The bulk of the evidence indicates that there is hard bargaining between processors and retailers on rebates but relations are not coercive. Retailers and wholesalers endeavour to buy as cheaply as possible from suppliers, so as to sell as cheaply as possible to consumers.

4. The small processor (whose sales volume is less than $10 million sales) is having a difficult time financially, particularly during the last three years. The large processor, on the other hand, is earning a reasonable net margin and return on equity.

5. Notwithstanding the conclusion in the paragraph above, there is no significant difference in rebate levels among differing sizes of firms when milk processors are excluded, although there are different patterns of use. Accordingly, there is no support for the theory that rebates are paid as a resolution of market power measured by the size of the firm, although market power or the size of a processor may be an important factor in financial performance.

6. There is no significant difference in rebate levels offered by suppliers controlled by retailers as compared with those not controlled by retailers.

CHAPTER 6 - MILK PROCESSORS AND REBATES

1. All raw milk in Ontario is marketed through the Ontario Milk Marketing Board. This Board establishes the price that milk processors are obliged to pay for the purchase of milk. As a result, the fluid milk shipper (the dairy farmer) does not offer rebates to market his product.

2. The number of dairies in Ontario has declined dramatically in the past 15 years as processing has become more centralized. Consumers now purchase their milk mainly from retailers and seldom by way of home delivery.

3. The rebate level on fluid milk offered by processors has increased significantly in the past few years to the point that volume rebate levels in 1979 ranged from 5% to 30%.

4. The major reason for the high level of rebates is price competition among the dairies. An additional reason is the savings due to large scale production. Dairies do not cost justify their levels of rebates, due to the expense of such a study.

5. A small retailer cannot buy milk as cheaply as a large retailer and consequently is at a disadvantage. Nevertheless, there has been no reduction in the number of outlets where a consumer can purchase milk.

6. Large retailers sell milk, in certain cases, at a loss or at a reduced price. Consumers are benefitting from the intense competition at both the processing and retailing levels.

7. A profit and equity survey of the four largest dairies indicates a low profit margin on sales of 1.5% and a reasonable return on equity of 15.5%. Therefore, payment of very high rebates by dairies does not appear to be associated with abnormally low (or high) profit levels among these processors.

8. I agree with the conclusion in the Milk Commission Report of 1975, that "in general, the marketing system for fluid milk is relatively efficient, progressive, flexible and equitable". However, I would suggest that the Milk Board should continually monitor the milk industry from dairy farmer to retailer to ensure that no serious aberrations develop.

CHAPTER 7 - BUYING GROUPS AND REBATES

1. Buying groups are formed by buyers to obtain the highest possible level of volume rebates from suppliers.

2. Except for a few large retailers who have sufficient purchasing power on their own, an important number of retailers in Ontario purchase through a buying group or from a member of a buying group.

3. Buying groups eliminate most differences in levels of volume rebates due to volume-purchasing differences between large and small retailers and wholesalers.

4. It may be difficult for a small retailer or a small wholesaler to become a member of a buying group because of the group's membership requirements.

5. Rebates received by buying groups from suppliers are passed through to members, and the groups operate on a non-profit basis.

6. The amount of volume rebates paid to buying groups may not correspond to the cost savings of volume ordering. The implications of this conclusion are stated in the following paragraphs.

7. The percentage level of volume rebates for all members of buying groups is approximately the same, regardless of the member's size.

8. The percentage level of volume rebates for buying group members may be similar to the level of volume rebates for the large chains which are not buying group members.

1. Wholesalers play a major role in the distribution of food. The Ontario wholesale food market accounted for approximately $4.0 billion in sales in 1979.

2. The sales of the 21 largest wholesale firms accounted for $1.9 billion of 1977 Ontario wholesale sales, or 58% of the estimated $3.3 billion of sales by all wholesalers.

3. Wholesalers surveyed operated on net after-tax profits of less than one per cent of sales. The surveys showed wholesalers' returns on equity varied from 5.8% to 15.9%. These returns are similar to those of other similar industries and indicate that rebates are not associated with abnormally low or high profits at the wholesale level.

4. Rebate levels for wholesalers averaged from 5% to 7% of purchases. These figures include estimates of off-invoice allowances.

5. All rebates received by wholesalers appear to be passed through, either directly or indirectly, to the retailers.

6. The size of rebates paid to the wholesaler does not seem to be directly related to the size of the wholesaler.

CHAPTER 9 - LARGE RETAILERS, CONSUMERS AND REBATES

1. The retail segment of the food industry is moderately to highly concentrated. It is estimated that the retail food chains, including convenience store chains, account for 73% of food sales in Ontario.

2. There is no significant difference in the cost of sales and profit levels between large and small chains.

3. Net profits (after tax) for large and small chains average 1% of sales. The return on equity (after tax) for small chains amounts to 18.3% compared to 16.1% for large chains.

4. All rebates, whether received by cheque or by off-invoice allowance, are reflected in the net profit figures of retailers.

5. Rebates are a major source of revenue to the retail chains. Rebates received by cheque amount to 2.48% of retailer sales. Off-invoice allowances approximate 3.5% of retailer sales. Therefore, all rebates received by retailers approximate 6% of sales.

6. Rebate levels have increased substantially in the past eight years.

7. The weighted average rebate level for small chains is 7.4%, and for large chains, 7.7%, of purchases.

8. The conclusions above indicate that chains receive approximately 6% of sales in rebates and receive a profit of 1% of sales. The consultants' reports on retailer accounting systems show that rebates either lower the net cost of goods to retailers or lower the net costs of retailer operations, both of which in turn lower the cost of goods to consumers. This conclusion, namely that rebates are used to lower the prices that consumers pay, is reinforced by the fact that the average return on equity (after tax) by the chains is 17.1%. This is, at best, an average rate of return when compared with non-food industries.

9. If rebating were to be disallowed, it would probably result in consumers' paying higher prices for food to consumer.

10. The evidence at the Inquiry indicated that there is a real and intense competition between the chains for market share. Volume turnover is the key to success when operating on a small profit margin. The chain buyers reflect this competition and endeavour to buy as cheaply as they can. In setting sale prices for food, the chains are attentive to the prices of competitors, and a major motivation is to increase sales so as to increase their market share.

11. The evidence indicated that Ontario retail chains operate more efficiently, as a whole, than other food chains in North America. This is reflected in the fact that Ontario food prices are the lowest in Canada.

CHAPTER 10 - SMALL RETAILERS AND REBATES

1. There is no exact definition of a small retailer. There are, in fact, seven types of stores which can be considered small retailers.

2. In Ontario, 7,702 stores are classified as small retailers and 689 as large retailers.

3. Most Ontario retail food sales are made by the large retailers.

4. Between 1969 and 1979, the market shares of group independents and unaffiliated independents declined sharply during the first six years of this period and more slowly during the last five.

5. There is no statistically significant difference in the gross margin, net margin after tax or return on equity between the large and small retailers sampled.

6. There is no significant difference in rebate levels between large and small retailers, when averages weighted according to product mix are considered.

7. The large retailer is presently not able to take advantage of the smaller retailer through the rebate mechanism, despite allegations to the contrary.

8. The data in evidence indicates that any retailer, regardless of size, may have high or low average rebate levels, but that small retailers benefit from the buying power of their wholesalers. Thus goods purchased by the small retailer, on average, carry the same rebate as similar goods purchased by the large retailer.

9. Smaller retailers have the following competitive advantages over the chains:

   (a) better knowledge of the product preferences of their customers;

   (b) more personalized service;

   (c) greater selling and buying flexibility;

   (d) lower wage scales;

   (e) greater ability to require suppliers to provide certain labour-related services;

   (f) more tax advantages;

   (g) absence of restrictions in regard to store hours.

10. The chains have the following competitive advantages over smaller retailers:

   (a) greater media advertising;

   (b) better understanding of the rebate system;

   (c) greater access to capital;

   (d) better store locations;

   (e) ability to offer wine to consumers.

11. Despite the disadvantages listed in the paragraph above and considering all aspects of the small retailer's operation, it does not appear that the small retailer is unable to compete with larger competitors. This conclusion is reinforced by the evidence of small retailers themselves in respect of their ability to compete. I will consider the qualification expressed by one retailer in Chapter 14, Loss-Leader Selling.

RECOMMENDATION

1. The ability of large retailers to sell wine appears to be an advantage enjoyed by the large retailers. It is recommended that the Legislature consider the feasibility of permitting small retailers to sell wine.

CHAPTER 11 - NAME BRANDS, HOUSE BRANDS AND REBATES

1. House brand products are sold by manufacturers to retailers for less than comparable name brand products. In turn, retailers charge consumers less for house brand products than for name brand products.

2. The average rebate level for name brand products is 10.6% of sales whereas the average rebate level for house brand products is 4.3% of sales.

3. Lower costs of production, advertising and selling result in both lower rebate levels granted by, and lower net selling prices paid to, manufacturers for house brand products relative to name brand products. Market factors, as well as lower costs, enable retailers to offer house brand products more cheaply to consumers than name brand products.

CHAPTER 12 - COST JUSTIFICATION OF REBATES

1. There are widely divergent views as to the need for legislation requiring the cost justification of rebates. I share the view of the Grocery Products Manufacturers that such a legislative requirement would inhibit the natural operation of a free market and would lead to reduced competition.

2. In general, all rebates have an element of cost justification in their origins, but considerably more market factors than cost savings enter into the final determination of a rebate level.

3. It is not feasible for this Commission to determine whether or not rebates are fully cost justified. Processors, wholesalers and retailers do not have accounting systems in place to provide the necessary information. For the Commission itself to attempt to acquire the necessary data would involve excessive time and expense.

4. The effect on the farmer of legislation requiring cost justification may be that competition among processors and retailers would be reduced. In this case, farm prices may be adversely effected.

5. Legislation requiring cost justification would burden processors with the task and expense of justifying price reductions. In this case, the expense would likely be passed through to the consumer and processors would become reluctant to reduce prices. If these assumptions are correct, consumer prices would be adversely affected.

CHAPTER 13 - CONCENTRATION AND REBATES

1. Concentration at the producer level ranges from atomistic (many sellers - many buyers) to monopolistic. Increasing values of farm products are subject to marketing boards, a unique type of monopoly sanctioned by the Legislature. The average farm size is increasing and barriers to entry in the form of capital investment requirements are higher than before. Therefore, I conclude that concentration at this level of the food chain appears to be increasing.

2. Concentration at the processor level is high and moderately high for many commodities. However, I conclude that discounting is not a cause of high degrees of concentration at the processor level because there is no correlation between the rebate levels and

the size of processors nor between rebate levels and financial performance of processors.

3. Concentration at the wholesaler level is moderately high and is characterized by an oligopoly of three corporations. However, I conclude that discounting is not a cause of the degree of concentration at the wholesaler level because there is no correlation between the rebate levels and the size of wholesalers. Furthermore, the degree of concentration in the wholesale market is not allowing the firms to earn higher than normal profits.

4. Concentration at the retailer level is moderately high. The degree of concentration has increased during the last ten years but there is significantly less of an increase during the last five years. I expect that future increases, if any, will likely be minimal due to the strength of various competitors in the Ontario retail food market. I conclude that discounting is not a cause of increasing concentration at this level because there is no correlation between the rebate levels and the size of retailers nor between rebate levels and financial performance of retailers.

1. There is no common definition of "loss leader"; the definition which I have chosen to use is: the reduction of price below the retailer's shelf cost which includes the retailer's net acquisition cost and all costs incurred up to the point where the food is sold to the consumer.

2. Staple food products are, from time to time, subject to loss-leader selling by major retailers. Such selling may stimulate increased pressure upon suppliers for reduced prices. Such selling certainly reduces the price of the product to the consumer and increases the sales of the farm products involved, at least in the short run. There is no evidence that retailers uniformly mark up prices on other products to compensate for losses incurred during the loss-leader sale.

3. Associations representing suppliers in three industries -- bakeries, milk distributors, and potato growers -- alleged that loss-leader selling has had a detrimental effect financially on their members. However, these industries have all undergone structural or market changes or deficiencies that may cause all or part of their distress. Therefore, I cannot conclude that the elimination of loss-leader selling would outweigh the present benefits of such selling to the consumer and to the farmer.

1. Listing allowances (also called "introductory allowances") are offered by suppliers to retailers in return for services performed and for risks borne by the retailer upon the introduction of a new product.

2. The amounts paid for such allowances do not appear to be unreasonable considering the cost and risk of new-product marketing to the retailer.

3. The allegation that manufacturers are delisted for failure to meet discounting demands has not been substantiated. The evidence of 24 major food manufacturers and of the major retail chains is, in fact, that products are delisted usually because of poor sales, not for discounting reasons.

4. The G.P.M.C., the manufacturers, and retailers were unanimous in their view that if a problem exists in the listing or delisting of products, it could best be solved in the market place without legislative interference.

1. The Combines Investigation Act does have shortcomings which prevents it from being as effective as it might be. I do not, however, subscribe to the opinion of some, expressed before me, that this legislation is vacuous and ineffective. On the contrary, there is evidence that the companies involved are quite aware of this legislation and endeavour to comply with it.

2. The Robinson-Patman Act, legislation controlling discounting in the United States, has serious defects which prevent it from being a suitable legislative model for this country. In addition, the testimony I have heard from all levels of the food industry was almost unanimous to the effect that more legislation is not desirable or advisable at the present time. Such comments were made not only by representatives of the larger firms, but also by representatives from that class of business which these proposals purportedly would protect: small- and medium-sized business.

3. In respect of the United States legislation, the Robinson-Patman Act, I have considered and rejected the importation into Canada of the stricter standard of liability which this legislation imposes. Even if I were convinced that small business needs a stricter standard to protect it from larger competitors, I am not convinced that the Robinson-Patman Act accomplishes this purpose. Indeed, I question whether this statute

does not unduly restrict the affairs of business in the United States and in so doing, result in higher prices for food products to the detriment of consumers.

4. In respect of the proposals submitted by the Ontario Federation of Agriculture and the Ontario Liberal Party, I would first like to express my appreciation to both these organizations for the effort and care put into advancing these proposals. On the other hand, I cannot recommend either of these proposals to the Ontario government. On the basis of the evidence submitted to this Commission, I do not find that the magnitude of the problem indicated by the evidence warrants the solutions proposed.

5. If this problem were in the future to become as grave as these two organizations believe it will, then the proper body to pass such legislation would be the Government of Canada and not the Government of Ontario. This is so because the problem they perceive is a problem of competition policy requiring an approach that integrates legislation related to discounts and legislation related to other aspects of competition as well. For example, I think it is quite possible that a retailer restricted as to its bargaining with suppliers would consider alternative means, such as vertical integration, of achieving the same ends. I do not think the Ontario Government has the jurisdiction or the effective means to apply and enforce the sanctions necessary to preserve competition in an economy where

companies transacting business on a national and international basis are the rule rather than the exception.

6. In order to meet the particular problems disclosed by the evidence in this inquiry, I recommend that the Ontario Government follow the path of arbitration rather than of legislation. My recommendation in this regard is expressed in Chapter 18.

CHAPTER 17 - FINDINGS OF OTHER INQUIRIES AND STUDIES

1. To a degree, it is beneficial to consider the conclusions arrived at by previous studies and inquiries. However, such conclusions are not always applicable to the present context due to differences in industry structures and marketing patterns which vary with time and market area.

2. I agree with the 1978 report of the British Columbia Select Committee that most previous investigations, but not all, have treated the subject of rebates in a superficial manner and have only added to the confusion surrounding this subject. I also concur with the recommendation in that report that no further studies of the food industry are necessary or desirable at the present time.

3. I agree with the findings of the 1977 Report of the Milk Commission of Ontario that the marketing system

for fluid milk in Ontario, a system in which rebates play an important role, is relatively efficient and equitable.

4. I agree with the Mallen Report's conclusion that there is no strong evidence that rebates have been a major contribution to concentration. I am unable to agree with Professor Mallen that concentration in Canadian food retail markets leads to prices higher than they should be, particularly in Ontario. However, in fairness to Professor Mallen, I must say that I have not studied this question in the depth that he has studied it, nor do my terms of reference permit me to do so.

CHAPTER 18 - OVERVIEW OF THE FOOD INDUSTRY

1. There is an undue amount of animosity between the various levels of the food chain in Ontario. This antagonism could eventually be detrimental to what is now an extremely efficient and inexpensive food distribution system.

RECOMMENDATION

1. In order to deal with this animosity, I recommend that the Government of Ontario constitute a forum of arbitration and mediation separate and apart from both government and any particular sector of the food industry.

APPENDIX 1

LIST OF WITNESSES

LIST OF WITNESSES

The following witneses appeared before the Commission:

Name	Position or Profession	Affiliation, if any
ABERMAN, Arnold	Note: Dr. Aberman is a medical doctor but appeared, however, as a concerned citizen on behalf of the Citizen's Coalition	Citizen's Coalition
ALLEN, Hilliard McKenzie	formerly, a dairy owner	Bolton Dairy
ANDREWS, Richard	owner	Scarborough Fair Convenience Store
APPLETON, John M.	Secretary-treasurer	Ontario Poultry Processors Assoc.
ARMSTRONG, Les	Secretary-manager	Ontario Fresh Potato Marketing Board
ARMSTRONG, Robert	Solicitor	on behalf of the Independent Milk Distributors Association
BARNES, Roy	National sales manager	General Foods Limited
BEBEN, Henry George	Vice-President of sales and marketing	J.M. Schneider Incorporated
BERTRAND, Raymond	President	Canadian Grocery Distributors' Institute
BERTRAND, Robert	Director of Investigation and Research, Assistant Deputy Minister of Competition Policy	Department of Consumer and Corporate Affairs, Government of Canada
BINNINGTON, Roland Melville	President	Beatrice Foods Ontario Limited
BOLTON, Thomas G.	Deputy Chairman, Board of Directors and Chief Executive Officer	Dominion Stores Limited
BRAS, Robert	Partner & President	Menu Foods

Name	Position or Profession	Affiliation, if any
BROOKS, Harold Joseph	Vice-President of Finance	Gay-Lea Foods Co-operative
CALBECK, Jack	President	R.M. Calbeck Limited
CARTER, J.P.	Vice-President and General Manager of the Food Division	Retail Council of Canada
CHALMERS, James Earl	Farmer, Chairman	Ontario Chicken Producers Marketing Board
CICERI, Wyne	Office Manager	Mitchell Pacific Limited
COHEN, Moe	President	Dominion Farm Produce
CROMPTON, George Alex	General Manager	Retail Merchants Association of Canada (Ontario) Incorporated
CULBERT, Gary	Director of Marketing	Canadian Canners Limited
DARRIGO, Frank	President	Ontario Produce Buyers Association
DAVIS, Donald L. Henry	Vice-President in charge of consumer products	Canada Starch Company
DAWSON, Gregory George	President	Stoney Creek Dairies
DAY, John Francis	Vice-President of Marketing	H.J. Heinz
DENNIS, Frank	Executive Vice-President of Operations	Kellogg-Salada Canada Inc.
DeSOUZA,	Food Broker	
DUBUC, Jean M.	National Sales Manager	Catelli Foods Limited
DUFFY, Michael Earl	President	Silverwood Dairies Limited
FERRI, Al	Apple Farmer	
FINGLER, Norman Donald	Toronto Zone Manager	Canada Safeway Limited

Name	Position or Profession	Affiliation, if any
FISHER, Ralph	Project Director	Laventhol & Horwath
GADD, Kenneth V.	General Manager	Canadian Federation of Retail Grocers
GARVEY, Bartley	Attorney, Bureau of Competition	Federal Trade Commission, Government of the United States
GRAHAM, Peter Allister	Vice-President, Food Divisions	Oshawa Group Limited
GRANT, Jon	President and Chief Executive Officer	Quaker Oats of Canada Limited
HAMILL, James	Assistant to the Director, Bureau of Competition	Federal Trade Commission, Government of the United States
HANNAM, Peter	President	Ontario Federation of Agriculture
HARWOOD, Kenneth Roy	Partner	J & K Farms
HEAGLE, Douglas Evans	Past President	Bakery Council of Canada
HERRICK, John D.	Chairman of the Board	General Mills, Canada Limited
HICKS, Allan Arthur	Director of Planning	Ontario Milk Marketing Board
HILL, William James	Grocer	Lakeshore Marketeria
HOLT, Geoffrey Cranston	President	Holt Grocery Distributors Limited
HOSKINS, Gregory	Marketing Services	Redpath Sugar Limited
INFELISE, Joseph	Vice-President Dairy Division	Gay-Lea Foods Co-operatives Limited
JACKSON, Allen C.	President	Dominion Stores Limited

Name	Position or Profession	Affiliation, if any
JACKSON, Janet	Past President of Ontario Association, Vice-President of National Association	Consumers Association of Canada
JEWSON, James Frederick	Vice-Chairman	Milk Commission of Ontario
KELLY, Robert Walter	General Manager	Meat Packers Council of Canada
KENNEDY, Edward Charles	Chairman of the Board and President	Great Atlantic and Pacific Company of Canada Limited
KINCAID, Leon Archibald	President	Standard Brands Food Company
KIRK, George L.	Vice-President of Marketing	Campbell's Soup Company Limited
LABROSSE, Leo	President	Atlantic Sugar Limited
LaRUE, Paul H.	Attorney	Chadwell, Kayser, Ruggles, McGee and Hastings (United States)
LACKIE, Herbert Keith	Advisor	Meat Packers Council of Canada
LENNIE, Peter Soutar	Chairman of the Board, President and General Manager	National Grocers Company Limited
LEVINE, Irving	Director of Buying and Sales	Darrigo Supermarkets
LEVINE, Jack	President	Steinberg, Incorporated
LONG, Gerald	Farmer, Chairman	Ontario Apple Marketing Commission
LUNAU, Douglas Norman	Vice-President, Intersave	Loblaws Limited
MACKIE, Douglas Robert	Vice-President and General Manager of the Dairy Division	Borden Company

Name	Position or Profession	Affiliation, if any
MAICH, Robert Samuel	President	Mac's Convenience Stores Limited
MALLEN, Bruce	Economist	
McEWAN, Murray	President	Redpath Sugars Limited
McGREGOR, Barney	Vice-President Consumers Products Division	Gay-Lea Foods Co-operative Ltd.
McGUIGAN, James	Apple grower and a Member of the Provincial Parliament	
McKAY, Robert	Vice-Chairman	Farm Products Marketing Board
McKICHAN, Alistair J.	President	Retail Council of Canada
McLAINE, Archie	Vice-President of Marketing	McCain Foods Limited
McLINDEN, Peter	Vice-President and General Manager	Gay-Lea Foods Co-operative Ltd.
MEDNICK, Howard	Consultant	Laventhol & Horwath
MORGAN, Jack	Food Broker	
MORLEY, David	President	Grocery Products Manufacturers Association of Canada
MOSSOP, Edward C.	Vice-President, Director of Marketing	Great Atlantic and Pacific Company of Canada Limited
MOYAL, Ralph	General Manager	Independent Wholesale Grocers Limited
NICHOL, David A.	President	Loblaws Limited
O'FLYNN, Maurice	Vice-President of Sales and Marketing	Green Giant of Canada Limited
ORR, George	Director of Services Branch, Bureau of Competition Policy	Department of Consumer and Corporate Affairs, Government of Canada

Name	Position or Profession	Affiliation, if any
PANOS, George	Vice-President and Buyer	Becker Milk Company Limited
PAPPAS, Paul Jordan	Vice-President, Produce Merchandising	Loblaws Limited
PAWLOWSKI, Jerry Joseph	Past President	Ontario Food Processors Association
	Co-owner	Stoney Point Canning Company Limited
QUARANTO, Carl	Store Owner	Sunshine Market
QUINN, Thomas B.	Vice-President, Director of Marketing and Sales	Kraft Limited
RICHARDSON, Mae Myrtle	Store Owner	Jubilee Center
ROBERTS, Edward J.J.	Executive Vice-President	Canada Packers Limited
ROSS, David	Consultant	Laventhol & Horwath
RUSSELL, Fred	Vice-President, Sales	Swift Canadian Company
RUTTAN, Arthur Oliver	Owner	Ruttan Foods Limited
SCOTT, Charles Earnest	President	Dominion Dairies Limited
SHAND, Barbara Jean	President	Consumers' Association of Canada (Ontario)
SHEBEC, Walter	Vegetable grower	
SINCLAIR, James William	Vice-President and General Counsel	Kellogg-Salada Canada Limited
SLINGER, Don	Vice-President	Ontario Poultry Processors Association
SMITH, John J.	Vice-President, Sales	Donlands Dairy Limited

Name	Position or Profession	Affiliation, if any
SMITH, Lorne	Comptroller	Becker Milk Company Limited
SMITH, Stuart	Member of Provincial Parliament, Leader of the Official Opposition	Ontario Liberal Party
SPELLISCY, Robert Glyn	Director, Vice-President, Treasurer, Manager of the Accounting Division	Canada Safeway Limited
SPITZER, Gerald	Vice-President and General Manager	Steinberg Incorporated
STAFF, Howard	Grape grower, President	Ontario Fruit and Vegetable Growers' Association
STAVRO, Steve	President and Owner	Knob Hill Farms
STOVEL, Robert	President	Stovel-Sienon Limited
TELFOR, James A.	Executive Vice-President, Operations	Maple Leaf Mills Limited
TIGERT, Donald	Financial Analyst	Burns, Fry Limited
TISDALL, Charles Woodland	President	Bakery Council of Canada
TOMA, John C.	Senior Vice-President, Marketing	Dominion Stores Limited
WARING, Brian Robert	Grocery Products Manager	St. Lawrence Corn Starch Company Limited
WARNOCK, Frank	President and Chief Executive Officer	M. Loeb, Limited
WEIR, Lloyd	President and Chief Executive Officer	Christie Brown and Company Limited
WEST, Ronald	Vice-President, Marketing	Zehrmart Limited
WIETFELDT, Richard Alan	Director of Research	Ontario Federation of Agriculture

Name	Position or Profession	Affiliation, if any
WILLIAMS, Douglas F.	Director formerly, Chairman	Farm Products Quality Branch, Ontario Food Council
WYGANT, James	President and Chief Executive Officer	General Bakeries Limited

APPENDIX 2

LIST OF EXHIBITS

LIST OF EXHIBITS

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
1.	Copy of the Order-in-Council dated August 23, 1978 constituting the Commission	Preliminary Hearing	2	December 7, 1978
2.	Copy of the notice of the preliminary hearing with attached list of publications in which the notice of preliminary hearing was published	Preliminary Hearing	2	December 7, 1978
3.	Copy of the notice of hearings prepared for advertisement in the "Farm and Country" publication	Preliminary Hearing	2	December 7, 1978
4.	Letter dated November 10, 1978, from Commission Counsel addressed to members of the food industry advising of the Commission's intentions respecting submissions.	Preliminary Hearing	4	December 7, 1978
5.	Letter with attached questionnaires dated December 1, 1978, from Commission Counsel addressed to certain retailers and processor/manufacturers	Preliminary Hearing	4	December 7, 1978
6.	Copy of the Order-in-Council dated February 7, 1979, appointing His Honour Judge Wilfred W. Leach to replace His Honour James F.W. Ross as Commissioner	1	4	February 14, 1979
7.	Copy of the notice of public hearings published in English language newspapers in Ontario during the first week of February, 1979.	1	4	February 14, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
8.	Copy of notice of public hearings published in French language newspapers in Ontario during the first week of February, 1979	1	4	February 14, 1979
9.	Letter with attached memorandum relating to concerns raised as a result of Commission investigations dated February 2, 1979, from Commission Counsel, addressed to members of the food industry	1	4	February 14, 1979
10.	Tentative Schedule of Sittings	1	5	February 14, 1979
11.	Brief dated February, 1979 submitted by the Ontario Federation of Agriculture, entitled "Address by Peter Hannam, President, The Ontario Federation of Agriculture to The Royal Commission on Discounts and Allowances"	1	11	February 14, 1979
12.	Copies of Farmer Price Index, a monthly publication of the Ontario Federation of Agriculture, dated February, 1978, to December, 1978, inclusive	1	20	February 14, 1979
13.	Chart entitled "Milk Discounts" extracted from the table illustrated at page 27 of Exhibit 15	1	22	February 14, 1979
14.	Chart entitled "Milk Discounts" extracted from the table illustrated at page 26 of Exhibit 15	1	26	February 14, 1979
15.	Brief dated February, 1979 submitted by the Ontario Federation of Agriculture, entitled "Brief to the Royal Commission on Discounts and Allowances presented by the Ontario Federation of Agriculture"	1	36	February 14, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
16.	Cheque stub #26760 of the Oshawa Group Limited and the Ontario Produce Co. Limited indicating various allowances deducted from the gross amount due Walter Shebec, during the period August 30, 1978 - September 29, 1978	2	16	February 15, 1979
17.	Cheque stub #31533 of the Oshawa Group Limited and the Ontario Produce Co. Limited indicating an allowance deducted from the gross amount due Walter Shebec during the period October 18, 1978 - November 14, 1978	2	16	February 15, 1979
18.	Brief dated February, 1979, submitted by Howard V. Staff, President of the Ontario Fruit and Vegetable Growers' Association entitled "Statement to the Royal Commission on Discounting and Allowances in the Food Industry in Ontario	2	50	February 15, 1979
19.	Letter with attached list of association membership dated November 21, 1978 from Frank Darrigo, President, Ontario Produce Buyers' Association addressed to Commission Counsel	3	64	February 19, 1979
20.	Brief, not dated, submitted on behalf of Messrs. M.J. Ferri and A. Ferri by A. Ferri	3	99	February 19, 1979
21.	Summary of discounts demanded by the I.G.A. Wallaceburg store prepared by the Hon. James McGuigan, M.P.P.	4	12	February 20, 1979
22.	Copy of a letter dated May 29, 1978, from McGuigan Orchards to M. Loeb (London) Ltd.	4	14	February 20, 1979
23.	Brief, not dated, submitted by James McGuigan M.P.P.	4	23	February 20, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
24.	Fact sheet dated June, 1978, produced for the Ministry of Agriculture and Food entitled "Ontario Agricultural Marketing Boards - 1978"	4	55	February 20, 1979
25.	Agreement for Marketing the 1978 Crop of Tomatoes for Processing an order made by the Farm Products Marketing Board under the Farm Products Marketing Act, dated February 24, 1978	5	3	February 20, 1979
26.	Copy of Bill 194: "An Act to amend and repeal certain Acts administered by the Ministry of Agriculture and Food" (proclaimed in force as of February 1, 1979)	5	23	February 21, 1979
27.	Brief dated December 29, 1978, submitted by Beatty and Wood, Barristers and Solicitors, on behalf of the Independent Milk Distributors Association entitled "The Discount/Rebate System, with Emphasis on Loss-leader Selling and Advertising of Milk and the Deteriorating Milk Distribution System in Ontario"	5	29	February 21, 1979
	Appendix 2, not dated, entitled "Declining Position of Members of I.M.D.A."	5	29	February 21, 1979
28.	Copy of Ontario Apple Marketing Commission Price Determination Order No. 007/78/79	6	6	February 22, 1979
29.	Report, dated February, 1977 by the Milk Commission of Ontario entitled "Inquiry on Wholesale and Retain Pricing Practices for Fluid Milk in Ontario 1971 to 1975"	6	33	February 22, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
30.	Memorandum dated February 21, 1979, from J.F. Jewson, Vice Chairman, Milk Commission of Ontario, to the Commission entitled "Activities of the Milk Commission of Ontario"	6	34	February 22, 1979
31.	Statement dated May 30, 1978, by J.J. Pawlowski, President, Ontario Food Processors Association, prepared for the Resources Development Committee	6	51	February 22, 1979
32.	Brief dated March 5, 1979 submitted by the Grocery Products Manufacturers of Canada entitled "GPMC Submission to the Inquiry into Discounting and Allowances in the Food Industry in Ontario	7	4	March 5, 1979
	Appendix B, no date, prepared by the Grocery Products Manufacturers of Canada entitled "Food Price Facts 1971-1978"	7	4	March 5, 1979
33.	Supplementary Data to the Grocery Products Manufacturers of Canada Brief to the Commission dated March 5, 1979, entitled "Food Manufacturing & Processing Industry Profits 1974-1978"	7	4	March 5, 1979
34.	Information dated February 6, 1979, published by the Center for the Study of Inflation and Productivity	7	30	March 5, 1979
35.	Study dated June, 1978, prepared by the Sector Task Force entitled "The Canadian Food and Beverage Industry"	7	33	March 5, 1979
36.	Brief dated March 5, 1979 submitted by Dominion Dairies Limited, entitled "Submission to the Inquiry into Discounting and Allowances in the Food Industry in Ontario"	7	104	March 5, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
37.	Issue of the publication Canadian Grocer dated February, 1978, entitled "1978 Food Brokers Issue and Market Survey"	8	28	March 6, 1979
38.	Study dated January, 1978, prepared by J.J. Singer Consulting Economists Limited for the Grocery Products Manufacturers of Canada entitled "The Canadian Food and Beverage Industry"	8	75	March 6, 1979
39.	Brief dated March 8, 1978 submitted by R.W. Kelly, entitled "Statement by W.R. Kelly, General Manager, Meat Packers Council of Canada to the Inquiry into Discounting and Allowaces in the Food Industry in Ontario - Toronto, March 8, 1979"	10	5	March 8, 1979
	with accompanying documents	10	5	March 8, 1979
40.	List of Ontario members of the Meat Packers Council of Canada	10	5	March 8, 1979
41.	Brief, not dated, submitted by John J. Smith, entitled "Opening Statement of John J. Smith, Vice-President, Donlands Dairy Co. Ltd."	10	44	March 8, 1979
42.	Brief dated March 12, 1979 submitted by the Ontario Poultry Processors Association entitled "An Introductory Statement by the Ontario Poultry Processors Association to the Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario"	11	4	March 12, 1979
43.	Study reprinted from the American Journal of Agricultural Economics, Volume 60, Number 5, December 1978, 1978, prepared by Thomas F. Funk and Martin T. Rice	11	24	March 12, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
	entitled "Effects of Marketing Boards on the Agribusiness Sector"			
44.	Brief dated March 12, 1979 submitted by Kraft Limited entitled "Statement by Kraft Limited to the Inquiry into Discounting and Allowances in the Food Industry"	11	43	March 12, 1979
45.	Brief dated March 12, 1978 submitted by I.A. Kincaid entitled "Presentation by Mr. I.A. Kincaid, President, Standard Brands Food Company to the Royal Commission on Discounts and Allowances"	11	66	March 12, 1979
46.	Copy of a letter dated February 20, 1979, from the Ontario Fruit and Vegetable Growers' Association addressed to the Commission listing commodities sold to the fresh market in Ontario not under provincial or federal marketing legislation	11	70	March 12, 1979
47.	Brief dated March 13, 1979, submitted by Kenneth V. Gadd, General Manager, Canadian Federation of Retail Grocers, entitled "Submission to the Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario by Kenneth V. Gadd"	12	72	March 13, 1979
48.	Four letters postmarked February 16 and February 20, 1979 returned to Canadian Federation of Retail Grocers from various independent stores in Ontario	12	73	March 13, 1979
49.	Four colour newspaper advertisements bearing dates of February 28, 1979 for products sold by Dominion Stores Ltd. and Loblaws Ltd.	12	73	March 13, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
50.	Brief dated March 14, 1979 submitted by Ruttan Diet Foods	13	34	March 14, 1979
51.	Letter dated December 21, 1978, from S. Jacobsen, Buyer/Merchandiser, The Oshawa Group Limited, addressed to Mr. Annett, National Sales Manager, Ruttan Foods Limited, requesting information as to the latter company's discounts, allowances and rebates	13	47	March 14, 1979
	Invoice dated February 21, 1979 from The Oshawa Group Limited ("Oshawa") addressed to Ruttan Diet Foods ("Ruttan") advising Ruttan that the amount of $700 would be deducted from Oshawa's next payment to Ruttan	13	47	March 14, 1979
52.	Letter dated March 9, 1979 from H.K. Leckie, Meat Packers Council to the Commission advising as to the content of photostatic copies enclosed	14	3	March 15, 1979
	Photostatic copy of Table 5: Farm Cash Receipts, 1976 to 1979, Ontario, extracted from the publication "Proceedings of the Canadian Agricultural Outlook Conference, 1978" published by Agriculture Canada	14	3	March 15, 1979
	Photostatic copy of page 10, a table indicating Farm Cash Receipts from Farming Operations, January - September, 1974-1978 extracted from the publication entitled "Farm Cash Receipts" published by Statistics Canada	14	3	March 15, 1979
	Photostatic copy of page 10, a table indicating Farm Cash Receipts from Farming Operations, January - December, 1974-1978 extracted from the publication entitled "Farm Cash Receipts" published by Statistics Canada	14	3	March 15, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
53.	Brief dated March, 1979, submitted by General Foods Limited, entitled "Submission to the Inquiry into Discounting and Allowances in the Food Industry in Ontario"	14	71	March 15, 1979
54.	Brief dated March 27, 1979, submitted by George E. Crompton General Manager, Retail Merchants Association of Canada (Ontario) Inc., entitled "Submission to the Royal commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario"	16	52	March 27, 1979
55.	Brief dated March, 1979, submitted by the Canadian Grocery Distributors' Institute entitled "Submission: Canadian Grocery Distributors' Institute to the Royal Commission in Discounting and Allowances in the Food Industry in Ontario"	17	3	March 28, 1979
56.	Letter dated March 16, 1979, from E.J. Roberts, Executive Vice-President, Canada Packers Limited, to the Commission listing the poultry farms owned by Canada Packers Limited and the acreage thereof	17	55	March 28, 1979
57.	Issue of the publication Maclean's dated March 19, 1979 containing an article at p. 38, entitled "More than the price is wrong"	18	30	March 29, 1979
58.	List of prices for Ontario dated March 19, 1979, submitted by Quaker Oats Co. of Canada Ltd. entitled "Price List No. 26, Area No. 4, south of an east-west line through and including Sioux Lookout and Hearst"	18	57	March 29, 1979
59.	1978 Annual Report of the Quaker Oats Company of Canada Limited	18	67	March 29, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
60.	Brief, not dated, submitted by Christie Brown and Company Limited, entitled "Statement of Christie Brown & Company Ltd. to The Royal Commission on Inquiry into Discounting and Allowances in the Food Industry in Ontario"	19	49	April 9, 1979
61.	Letter dated March 28, 1979 from Robert D. McCluggage, Solicitor for Redpath Industries to the Commission advising as to Redpath Sugar Limited's price lists for the weeks of March 19 and March 26, 1979, attached	19	65	April 9, 1979
62.	Calculation of processors' cost for raw milk processed into two per cent milk dated March 30, 1979 submitted by Robert J. Armstrong, Barrister and Solicitor, on behalf of the Independent Milk Distributor's Association	20	42	April 10, 1979
63.	Brief dated April 11, 1979 submitted by Frank M. Warnock, President and chief executive officer, entitled "M. Loeb, Limited Submission to the Inquiry into Discounting and Allowances in the Food Industry in Ontario"	21	30	April 11, 1979
64.	Brief dated April 11, 1979 submitted by Frank M. Warnock, President and chief executive officer, entitled "M. Loeb, Limited Submission to the Inquiry into Discounting and Allowances in the Food Industry in Ontario" with Exhibit A: Statistical data attached	21	41	April 11, 1979
65.	Brief dated March 13, 1979 submitted by The Ontario Federation of Agriculture entitled "Memorandum to the	22	3	April 12, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
	Royal Commission on Discounting and Allowances in the Food Industry in Ontario: Why there is discounting rather than bottom-line bargaining."			
66.	Statement dated October 23, 1978, prepared by Frank M. Warnock for presentation to the Canadian Federation of Retail Grocers	22	63	April 12, 1979
67.	Brief dated April 17, 1979 submitted by the Ontario Chicken Producers Marketing Board, entitled "A Presentation by the Ontario Chicken Producers Marketing Board to the Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario."	23	3	April 17, 1979
68.	Brief dated April 17, 1979, submitted by Peter Lennie, entitled "Opening Statement of Peter Lennie, President National Grocers Division of Loblaws Limited to the Royal Commission on Discounting and Allowances in the Food Industry in Ontario"	23	13	April 17, 1979
69.	Black-and-white newspaper advertisement bearing date of March 14, 1979, for products sold by Red & White stores	23	26	April 17, 1979
70.	Product Information Form of the Becker Milk Company Limited	24	17	April 18, 1979
71.	Brief dated April, 1979 submitted by the Consumers' Association of Canada Limited (Ontario), entitled "Submission to the Inquiry into Discounting and Allowances in the Food Industry in Ontario"	25	23	April 19, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
72.	Brief dated April 5, 1979 submitted by Lumsden Brothers Limited	26	3	April 20, 1979
73.	Brief dated April 19, 1979 submitted by the Ontario Federation of Agriculture, entitled "Memorandum to the Royal Commission on Discounting and Allowances in the Food Industry in Ontario: Data Questionnaires"	26	3	April 20, 1979
74.	Letter dated April 18, 1979 from B.R. Wareing, Sales Manager, Grocery Products, St. Lawrence Starch Company, to the Commission, advising as to the company's price sheet dated April 10, 1978, attached	26	4	April 20, 1979
75.	Photostatic copy of an article from the publication Kitchener - Waterloo Record dated October 27, 1976, entitled "Food Chains use bribes, blackmail, salesman charges" by Jim Romahn, Record staff writer	26	14	April 20, 1979
76.	Photostatic copy of the program of a convention held under the auspices of the Canadian Federation of Retail Grocers bearing date of October 25 and October 26, 1976	26	17	April 20, 1979
77.	Brief dated April 20, 1979, submitted by The Oshawa Group Limited, entitled "Submission to The Province of Ontario Royal Commission of Inquiry into Discounting and Allowances in the Food Industry"	26	34	April 20, 1979
78.	Letter dated April 11, 1979, from J.W. Rowley, Counsel for the Grocery Products Manufacturers of Canada, to the Commission advising as to the compilation of data attached,	27	4	June 11, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
	obtained by Coopers & Lybrand submitted December 14, 1978, respecting responses to the question "Have you ever had any product or products delisted because you refused to offer a discount, rebate or allowance?"			
79.	Brief, not dated, submitted by The Great Atlantic and Pacific Company of Canada Limited, entitled "Submissions to the Inquiry into Discounting and Allowances in the Food Industry in Ontario - Response to Commission Questionnaire - January, 1979"	27	5	June 11, 1979
80.	Organization Chart of Steinberg, Inc.	28	5	June 13, 1979
81.	Brief dated June, 1979, submitted by Steinberg Inc., entitled "Submission to the Inquiry into Discounting and Allowances in the Food Industry in Ontario"	28	5	June 13, 1979
82.	Product Information form of Steinberg, Inc.	28	34 65	June 13, 1979
83.	1978 Annual Report of Steinberg, Inc.	29	18	June 14, 1979
84.	Brief dated June 18, 1979 submitted by Canada Safeway Limited, entitled "Written Submission of Canada Safeway Limited to the Inquiry into Discounting and Allowances in the Food Industry in Ontario"	30	8	June 18, 1979
85.	Memorandum dated June 14, 1979, from Commission Counsel to the Commissioner respecting Public Inquiry Act Rulings	32	3	June 20, 1979
86.	Memorandum dated June 14, 1979 from Commission Counsel to the Commissioner respecting Public Inquiry Act Rulings as amended by Counsel	32	4	June 20, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
87.	Brief dated June 20, 1979 submitted by David A. Nichol, President, Loblaws Limited, entitled "A Submission to the Inquiry into Discounting and Allowances in the Food Industry in Ontario"	32	4	June 20, 1979
88.	Organization Chart of George Weston Limited, dated May 31, 1979	32	74	June 20, 1979
89.	1978 Annual Report of Loblaw Companies Limited	33	3	June 21, 1979
90.	List of co-operative advertising packages offered by Loblaws Limited Ontario Division	33	3	June 21, 1979
91.	Colour newspaper advertisement bearing date of June 6, 1979, for products sold by Loblaws Limited, Ontario Division	33	32	June 21, 1979
92.	Colour newspaper advertisement bearing date of June 13, 1979, for products sold by Loblaws Limited, Ontario Division featuring at pages L4 and L5 an advertisement for no-name eggs	33	37	June 21, 1979
93.	Colour newspaper advertisement bearing date of May 30, 1979, wherein Loblaws Limited, Ontario Division, offers coupon for use in connection with purchase of Tide laundry detergent	33	39	June 21, 1979
	Newspaper advertisement bearing date of May 30, 1979 wherein Dominion Stores Limited offers to redeem Tide coupons of any major competition	33	39	June 21, 1979
94.	Estimations of food sales by the Loblaw Group in Canada for the years 1977 and 1978, prepared by J. Donald Tigert, Burns Fry Limited	34	4	June 25, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
95.	Letter dated June 22, 1979 from James M. Murray, Counsel for the Ontario Federation of Agriculture, to the Commission, advising as to questions to be asked of chain stores	34	5	June 25, 1979
96.	Estimation of Loblaws Limited's milk rebates on a percentage of sales, prepared by the Ontario Federation of Agriculture	34	5	June 25, 1979
97.	List of suppliers of Ontario fruits and vegetables for 1978, submitted by The Great Atlantic and Pacific Company of Canada, Limited	34	24	June 25, 1979
98.	Product Information Form of The Great Atlantic and Pacific Company of Canada Limited	34	50	June 25, 1979
99.	Form of a co-operative advertising package for 1978 offered by The Great Atlantic and Pacific Company of Canada, Limited	34	50	June 25,
100.	Product Information Form indicating volume allowances and co-operative allowances of the Great Atlantic and Pacific Company of Canada Limited	34	50	June 25, 1979
101.	Issue of the publication Canadian Grocers dated February, 1979, entitled "1979 Food Brokers Issue & Market Survey"	34	63	June 25, 1979
102.	Organization Chart for Dominion Stores Limited dated March 19, 1979	35	3	June 26, 1979
103.	Brief dated December 29, 1978, submitted by Dominion Stores Limited, entitled "Brief to the Province of Ontario Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario"	35	3	June 26, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
104.	Brief, not dated, submitted by Dominion Stores Limited entitled "Statement on Behalf of Dominion Stores Limited"	35	3	June 26, 1979
105.	1978 Annual Report of Dominion Stores Limited	35	3	June 26, 1979
106.	Recap of lines discontinued by Dominion Stores Limited during 1978 and 1979	35	15 18	June 26, 1979
108.	Summary of Brief, Exhibit No. 109, submitted by the Retail Council	37	3	August 7, 1979
109.	Brief dated August, 1979 submitted by the Retail Council of Canada, entitled "Submission to: Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario:	37	3	August 7, 1979
110.	Revised footnotes to Brief, Exhibit No. 109	37	8	August 7, 1979
111.	Data respecting Ontario retail food chains, submitted by J. Donald Tigert, prepared for the Commission	38	12	August 8, 1979
112.	Data respecting Canadian retail food chains and food manufacturers, submitted by J. Donald Tigert, prepared for Food Media Conference held on October, 1978	38	12	August 8, 1979
113.	Letter dated June 28, 1979 from James H. Farrell, Vice-President and General Counsel, Loblaws Limited, advising as to amounts of various discounts, allowances and rebates received by Loblaws Limited, Ontario Division, during 1978	38	54	August 8, 1979
114.	Data respecting estimated sales percentage of particular commodities for Loblaws Ltd., Ontario Division, during 1978	38	55	August 8, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
115.	Brief, not dated, submitted by Dominion Farm Produce	39	4	August 9, 1979
116.	Brief dated August 3, 1979, submitted by Holt Grocery Distributors Ltd., entitled "Presentation to The Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario - Re: <u>Volume Incentive Allowances</u>"	39	42	August 9, 1979
117.	Data respecting amounts of various discounts, allowances and rebates recived by Dominion Stores Limited during 1978	44	4	August 10, 1979
118.	Letter dated July 10, 1979 from C.R. Brennecke, Vice-President and Comptroller, Dominion Dairies Limited, advising as to the company's discounting practices with Steinberg's Miracle Mart Stores and as to the company's price list effective April 30, 1979, attached	41	4	August 21, 1979
119.	Letter dated July 31, 1979 from Mitchell L. Wasik, Vice-President and Secretary, Dominion Stores Ltd., advising as to the responses to questions posed by the Ontario Federation of Agriculture, Exhibit No. 95	41	4	August 21, 1979
120.	Data respecting product lines delisted by Dominion Stores Limited	41	4	August 21, 1979
121.	List of co-operative advertising packages offered by Dominion Stores Limited	41	4	August 21, 1979
122.	Letter dated August 10, 1979 from Tim Carter, Vice-President and General Manager of The Food Division, Retail Council of Canada, to the Commission advising as to references to retail chains' efficiency and productivity	41	5	August 21, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
123.	Letter dated August 13, 1979, from Ken Gadd, General Manager, The Canadian Federation of Retail Grocers, to the Commission advising as to the sale of wine in Ontario	41	6	August 21, 1979
124.	Letter dated August 3, 1979 from Arthur M. Gans, Counsel for The Great Atlantic & Pacific Co. of Canada Limited, to the Commission, advising as to the answer to questions posed during the testimony of Edward Kennedy before the Commission on June 26, 1979	41	6	August 21, 1979
125.	Photostatic copy of an article from the publication <u>The Financial Post</u> dated September 6, 1975, entitled "Egg business needs a better break" by Arnold Aberman	41	87	August 21, 1979
126.	Photostatic copy of an article from the publication <u>The Financial Post</u>, not dated, entitled "Milk and medical projects win new enterprise awards"	41	87	August 21, 1979
127.	Brief, not dated, submitted by Arnold Aberman on behalf of The Citizens' Coalition, entitled "Submission to the Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario"	41	87	August 21, 1979
128.	Letter dated August 27, 1979 from Ralph Moyal, General Manager, Independent Wholesale Grocers Limited, to the Commission, advising as to the amount of volume rebates received by the company's Ontario members in 1978	43	3	Sept. 25, 1979
129.	Letter dated September 4, 1979 from Ralph Moyal, General Manager, Independent Wholesale Grocers	43	3	Sept. 25, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
	Limited, to the Commission advising to the company's list of members attached			
130.	Letter dated August 25, 1979 from Norman Fingler, Toronto Zone Manager, Canada Safeway Limited, to the Commission, advising as to dairies supplying Safeway Stores in Ontario	43	4	Sept. 25, 1979
131.	Letter dated September 14, 1979 from James H. Farrell, Vice-President and General Counsel, Loblaws Limited, advising as to the answer to questions posed during the testimony of David A. Nichol before the Commission on August 8, 1979	43	4	Sept. 25, 1979
132.	Brief, not dated, submitted by Robert Bertrand, Director of Investigation and Research, Combines Investigation Act, Consumer and Corporate Affairs Canada, entitled "Re: Inquiry into Discounting and Allowances in the Food Industry in Ontario"	43	5	Sept. 25, 1979
133.	Brief dated September 26, 1979, submitted by Douglas E. Williams, formerly Chairman of the Ontario Food Council, entitled "Statement to Public Inquiry on Rebates and Discounts"	44	3	Sept. 26, 1979
134.	Copy of a statute entitled "The Ontario Producers, Processors, Distributors and Consumers Food Council Act", Revised Statutes of Ontario 1970, Chapter 238	44	4	Sept. 26, 1979
135.	Photostatic copy of two telecommunications, one dated May 18, 1979, one dated August 1, 1979 from G.D. Robinson, and W.C. Nicolson, respectively of Kellogg-Salada Canada Inc. to R. Buckland of the company advising as to the reasons for the company's declining sales	44	33	Sept. 29, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
	to Dominion Stores Limited in 1962			
136.	Photostatic copy of a letter dated August 9, 1979, from G.D. Robinson of Kellogg-Salada Canada Inc. to R. Buckland of the Company advising as to the autonomy of the company's Canadian operation	44	36	Sept. 29, 1979
137.	Brief dated July, 1979 submitted by The Canadian Conference of Teamsters, The Bakery Council of Canada and The Retail Merchants Association of Canada Inc.	44	40	Sept. 26, 1979
138.	Report dated September, 1979, prepared by the Bakery Council of Canada and the Canadian Conference of Teamsters to the Loss Leader Committee	44	40	Sept. 26, 1979
139.	Brief dated September 27, 1979 submitted by Stuart Smith M.P.P., entitled "Statement by Dr. Stuart Smith, M.P.P. Leader of the Official Opposition to the Royal Commission on Discounts and Allowances in the Food Industry in Ontario"	45	17	Sept. 27, 1979
140.	Report dated February, 1976 prepared by Bruce Mallen, Ph.D., entitled "Reference Paper No. 6: A Preliminary Paper on The Levels, Causes and Effects of Economic Concentration in the Canadian Retail Food Trade: A Study of Supermarket Market Power"	46	106	October 9, 1979
141.	Guides for Advertising Allowances and Other Merchandising Payments and Services, promulgated May 29, 1969, as amended August 4, 1972, prepared by The Federal Trade Commission of the United States Government	47	72	October 11, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
142.	Photostatic copy of a chart entitled "Bureau of Competition: Formal Investigations - Robinson-Patman Act" listing initiations and dispositions during the period 1965 - 1974, extracted from Page 127 of a report of the Ad Hoc Subcommittee on Antitrust, the Robinson-Patman Act, and Related Matters of the Committee on Small Business, House of Representatives of The United States Government entitled "Recent Efforts to Amend or Repeal the Robinson-Patman Act"	47	73	October 11, 1979
143.	Photostatic copy of a chart entitled "Robinson-Patman Actions: 1974-1979" listing initiations and dispositions during the period 1974-1979, submitted by the Federal Trade Commission of the United States Government	47	73	October 11, 1979
144.	Issue of the Publication Trade Regulation Reports dated October 4, 1978, listing antitrust cases commenced, for the twelve month period ending June 30, 1960-1977, at page 12, Table 28 thereof	47	101	October 11, 1979
145.	Report, not dated (publication date 1977), prepared by the United States Department of Justice, entitled "Report on the Robinson-Patman Act"	47	106	October 11, 1979
146.	Brief dated October, 1979 submitted by Laventhol and Horwath, entitled "Brief Analysis for the Royal Commission of Inquiry into Discounting and Allowances in the Food Industry in Ontario"	48	3	October 23, 1979
147.	Biographies of Laventhol and Horwath staff who participated in the preparation of Exhibit #146	48	4	October 23, 1979

	Description of Exhibit	Volume of Transcript	Page Number	Date Admitted
148.	Memorandum dated October 10, 1979, from Robert Weist of the Commission, respecting discounting during the 1979 growing season	48	20	October 23, 1979
149.	Photostatic copy of a Table indicating Ontario Farm Cash Receipts during 1977 extracted from page 3 of a study entitled "Sales of Ontario Farm Products Through Marketing Boards, Chain Stores and Other Outlets" dated October 22, 1979, prepared by the Economics Branch, Ministry of Agriculture and Food, for the Commission	48	21	October 23, 1978
150.	Brief dated October, 1979, submitted by the Ontario Federation of Agriculture entitled "Brief to the Royal Commission on Discounts and Allowances"	49	3	October 24, 1979

APPENDIX 3

ONTARIO BUYING GROUPS

BUYING GROUPS INVOLVING ONTARIO WHOLESALERS AND RETAILERS

...as of December 31, 1979

INDEPENDENT WHOLESALE GROCERS LIMITED (I.W.G.L.) (Concord, Ontario)

Bennett Foods Limited (Kingston)

A.H. Boulton Company Limited (Windsor)

R.M. Calbeck Limited (Brantford)

D'Arrigo's Supermarkets Limited (Toronto)

Elliott Marr and Company Limited (London)

Gamble Robinson Limited (Toronto)

Knechtel Wholesale Grocers Limited (Kitchener)

Lanzarotta Wholesale Grocers Limited (Concord)

Thomson Groceries Limited (Toronto)

U.B.A. Trading Company Limited (Toronto)

G.E. Barbour Company Limited (New Brunswick)

Capitol Stores Limited (Nova Scotia)

Consolidated Grocers Limited (British Columbia)

Cooper's Discount Foods Limited (Newfoundland)

Deblois Brothers Limited (Prince Edward Island)

G. and H. Marketing Enterprises Limited (British Columbia)

Lewisporte Wholesalers Limited (Newfoundland)

Mayrand Limitée (Quebec)

Morris Wholesale Limited (New Brunswick)

M.A. Powell Limited (Newfoundland)

A.L. Raymond Limitée (Quebec)

Robin Jones and Whitman Limited (Quebec)

Royal Grocery Limited (Newfoundland)

Scotia Wholesale Limited (Nova Scotia)

J.P. Vincent and Freres Limitée (Quebec)

UNITED GROCERY WHOLESALERS LIMITED (U.G.W.L.) (Alberta)

The Great Atlantic and Pacific Company of Canada Limited (Toronto)

Alberta Grocers Wholesale Limited (Alberta)

Associated Grocers Limited (Alberta)

Associated Merchants Limited (British Columbia)

Co-op Atlantic (New Brunswick)

Federated Co-operatives Limited (Saskatchewan)

Four-Way Wholesale Limited (Alberta)

Merchants Consolidated Limited (Manitoba)

Merco Wholesale Limited (Alberta)

Overwaitea Foods (British Columbia)

Slade & Stewart Limited (British Columbia)

Sobey's Stores Limited Limited (Nova Scotia)

Woodward Stores Limited (British Columbia)

I.G.A. CANADA LIMITED (Toronto)

M. Loeb Limited (Ottawa)

The Oshawa Group Limited (Toronto)

Bolands (Nova Scotia)

The Codville Company (Manitoba)

Horne & Pitfield Foods Limited (Alberta)

Hudon et Deaudelin Limitée (Quebec)

FOODWIDE OF CANADA (1977) LIMITED (Toronto)

Loblaws Limited (Toronto)

National Grocers Company Limited (Toronto)

Zehrmart Limited (Kitchener)

Atlantic Wholesalers (New Brunswick)

L.H. Chernin & Sons Limited (Nova Scotia)

Kelly Douglas & Company Limited (British Columbia)

Provigo Incorporated (Quebec)

Westfair Foods Limited (Manitoba)

INTERSAVE (DIVISION OF LOBLAWS COMPANIES LIMITED (Toronto)

Loblaws Limited (Toronto)

National Grocers Company Limited (Toronto)

Zehrmart Limited (Kitchener)

Atlantic Wholesalers (New Brunswick)

Kelly Douglas & Company Limited (British Columbia)

Westfair Food Limited (Manitoba)

INTERNATIONAL TOBACCO WHOLESALERS ALLIANCE LIMITED (I.T.W.A.L.) (Mississauga)

Though this buying group deals with products normally sold by a supermarket - tobacco, confectionaries and beverages - its wholesaler members do not carry a full line of grocery products and for this reason, its 163 members are not listed here.

RETAIL MERCHANTS ASSOCIATION OF CANADA (ONTARIO) INC. (SCARBOROUGH)

This buying group has approximately 4,500 retailer members, of which approximately 2,500 sell food in some form. Naturally limitations of space prevent us from listing the entire membership. Generally speaking members are independent, small retailers including convenience stores, grocery stores and some combination stores.

APPENDIX 4

PROCESSOR/MANUFACTURER QUESTIONNAIRE

PROCESSOR/MANUFACTURER QUESTIONNAIRE

1. Please supply financial statements for the last three (3) years.

NAME-BRAND PRODUCTS

2. How many name-brand products do you sell, and what percentage of your total name-brand dollar sales does each represent?

3. Please list your top ten (10) name-brand products in terms of dollar sales in the past year.

4. For each of the products listed in 3 above, please detail for the past year;

   (a) gross sales in units;

   (b) gross sales in dollars;

   (c) all discounts, allowances, rebates and any other forms of payment showing total paid in dollars or otherwise, where appropriate;

   (d) for c) above please indicate the breakdown for retailers, independent grocers, franchise stores, etc. If possible, identify the geographic locatio of each (i.e. Southwestern Ontario, Metropolitan Toronto, Ottawa - Kingston - Peterborough, etc.).

5. (a) Please provide a written description for each of the discounts, allowances, rebates, etc. identified in 4 c) above.

   (b) How are these discounts, allowances and rebates forwarded (i.e. as a deduction from invoice or statement, as a credit note, as a separate cheque or in some other manner).

HOUSE-BRAND PRODUCTS

6. How many house-brand products do you sell, and what percentage of your total house-brand dollar sales does each represent?

7. Please list your top ten (10) house-brand products in terms of dollar sales in the past year.

8. For each of the products listed in 7 above please detail for the past year:

   (a) gross sales in units;

   (b) gross sales in dollars;

   (c) all discounts, allowances, rebates and any other form of payment showing total paid in dollars or otherwise, where appropriate;

(d) for c) above please indicate how much relates to retailers, independent grocers, franchise stores, etc. If possible, identify the geographic location of each (i.e. Southwestern Ontario, Metropolitan Toronto, Ottawa - Kingston - Peterborough, etc.).

9. (a) Please provide a written description for each of the discounts, allowances, rebates, etc. identified in 8 c) above.

(b) How are these discounts, allowances, and rebates forwarded (i.e. as a deduction from invoice or statement, as a credit note, as a separate cheque, or in some other manner).

10. For each of the products listed in 7 above, please detail:

(a) the current average price per product to retailers;

(b) a comparative name-brand product and its current average price to retailers.

11. Please provide arguments and/or financial figures justifying the differences between the prices of the name-brand and house-brand products as reflected in 10 above.

GENERAL

12. Please provide a written description of the impact of house-brand products on the nature of your business, over the past three (3) years.

APPENDIX 5

RETAILER QUESTIONNAIRE

RETAILER QUESTIONNAIRE

1. Please supply your company's financial statements for the last three years.

NAME-BRAND PRODUCTS

2. Please identify based on general observations (not statistically researched) the top selling national-brand(1) product(2) from Ontario suppliers(3) in each of the following categories, and list the name of the supplying company:

Baked Goods - i.e. bread
Beverages - i.e. soft drinks, juices
Canned Fruits - solids
Canned Vegetables - solids
Cereals - hot or cold breakfasts
Dairy Products - i.e. milk, eggs
Fresh Produce - grown in Ontario
Frozen Foods - i.e. fish, frozen orange juice, cakes
Meat - pre-packaged - i.e. bacon, sausage, poultry
Soups - canned or dehydrated

3. For each of the Ontario suppliers identified by yourself in 2 above please detail for your last fiscal year:

(a) gross purchases of name-brand products in dollars;

(b) gross purchases of house-brand products in dollars;

(c) all discounts, allowances, rebates and any other forms of payment or service showing total received in dollars or otherwise, where appropriate.

4. (a) Please provide a written description for each of the discounts, allowances, rebates, etc. identified in 3(c) above.

(b) How are these discounts, allowances, and rebates received (i.e. as a deduction from invoice or statement, as a credit note, as a separate cheque or in some other manner).

HOUSE-BRAND PRODUCTS

5. Please identify based on general observations (not statisically researched) the top selling housebrand(4) product(2) from Ontario suppliers(3) in each of the following categories, and list the name of the supplying company:

---

(1) National-brand is name brand.
(2) Individual consumer buying unit.
(3) An Ontario supplier is defined as having its billing address in Ontario.
(4) This includes generics and private-label brands.

Baked Goods - i.e. bread
Beverages - i.e. soft drinks, juices
Canned Fruits - solids
Canned Vegetables - solids
Cereals - hot or cold breakfasts
Dairy Products - i.e. milk, eggs
Fresh Produce - grown in Ontario
Frozen Foods - i.e. fish, frozen orange juice, cakes
Meat - pre-packaged - i.e. bacon, sausage, poultry
Soups - canned or dehydrated

6. For each of the Ontario suppliers identified by yourself in 5 above, please detail for your last fiscal year:

   (a) gross purchases of name-brand products in dollars;

   (b) gross purchases of house-brand products in dollars;

   (c) all discounts, allowances, rebates and any other forms of payment or service showing total received in dollars or otherwise, where appropriate.

7. (a) Please provide a written description for each of the discounts, allowances, rebates, etc. identified in 6(c) above.

   (b) How are these discounts, allowances, and rebates received (i.e. as a deduction from invoice or statement, as a credit note, as a separate cheque or in some other manner).

GENERAL

8. For each of the products listed in 5 above, please detail in the Metropolitan Toronto area:

   (a) the current average price per product to consumers and indicate the date taken;

   (b) a comparable Ontario-supplied name-brand product and its current average price to consumers taken on the same date as 8(a) above.

9. Please provide arguments and/or financial figures justifying the differences between the prices of the name-brand and house-brand products as reflected in 8 above.

10. Please provide a cost justification for the co-operative advertising schemes given to your suppliers.

APPENDIX 6

SAMPLE OF MANUFACTURER'S VOLUME REBATE SCHEDULE

PAYMENT SCHEDULE

EARNED COST REDUCTION PROGRAM

PRODUCT "X"

1978

Case Purchase [illegible]eau	Earned Rate
250,000 cases plus	65¢
175,000 - 249,999	60¢
155,000 - 174,999	55¢
135,000 - 154,999	50¢
115,000 - 134,999	45¢
90,000 - 114,999	40¢
65,000 - 89,999	35¢
10,000 - 64,999	30¢
Under 10,000	20¢

PLAN DETAILS:

1) All grocery accounts in Canada will have an opportunity to participate in this Earned Cost Reduction Program, through either direct involvement with Standard Brands or involvement with their supplier of Standard Brands merchandise. Independent stores or members of groups will participate in this Program in accordance with their agreement with the supplying wholesaler.

2) The program will be applicable to all 1978 case volume sales for "Product X".

3) Payments will be made to individual accounts by cheque on a Quarterly basis. The rate of payment will be based on estimated annual volume for each account, with any over-estimation or under-estimation compensated for in the Fourth Quarter.

4) The Program is by brand. The account will not be able to lump together "Product X" and "Product Y" to achieve a higher case plateau.

THIS PROGRAM IS SUBJECT TO CANCELLATION WITH 30 DAYS NOTICE.

APPENDIX 7

SAMPLE OF RETAILER'S CO-OPERATIVE ADVERTISING PROGRAM

To: All Suppliers
Attention: Sales Representative

Dear Sir:

Please find attached, a copy of our co-operative advertising promotional packages effective January 1, 1979.

We are not actively selling these promotions, however, if your company or the companies you represent, have monies to spend and you wish to purchase one of the promotions, I would ask that you contact my secretary, so that an appointment may be set up to discuss this matter.

Please read this over carefully and acquaint yourself with the package offerings.

Yours very truly,

CANADA SAFEWAY LIMITED

CO-OPERATIVE ADVERTISING AND DISPLAY

PROMOTIONAL PACKAGES 1979

Effective January 1, 1979, the following promotional packages will be available in the Toronto Zone Safeway Stores.

NO. 1 PROMOTION - Amount of store display space, newspaper space, number of items and cost to be negotiated. This multi-package promotion will be booked on a very limited basis.

NO. 2 PROMOTION - Includes 1 ITEM ONLY.
$2,500.
This package consists of a FULL END or equivalent floor display in all Class 'A' Stores and half end display or equivalent floor display in all Class 'B' Stores.

NO. 3 PROMOTION - Includes 1 ITEM ONLY.
$1,500.
This package promotion consists of a HALF END display or equivalent display in all Class 'A' Stores and where possible in Class 'B' Stores.

NO. 4 PROMOTION - Includes 1 ITEM ONLY.
$1,000.
This package promotion consists of a DUMP BIN or EXTRA DISPLAY in all Class 'A' Stores and where possible in Class 'B' Stores.

NO. 5 PROMOTION - Includes 1 ITEM ONLY.
$500.
This package promotion consists of a SHELF TALKER only in all Class 'A' and 'B' Stores and does not include specific displays. THIS PROMOTION DOES NOT INCLUDE ADVERTISING IN MAJOR NEWSPAPERS.

NO. 6 PROMOTION - Includes 1 ITEM ONLY.
$700.

(a) HEALTH & BEAUTY AIDS
This promotion consists of a SHELF TALKER in all Class 'A' and 'B' Stores and a newspaper advertisement. Extra promotional activity negotiable.

(b) FROZEN FOODS & PERISHABLES
The promotion consists of a HALF END MERCHANDISER or EXTRA DISPLAY in all Class 'A' Stores and a SHELF TALKER in all Class 'B' Stores. A FULL END MERCHANDISER is negotiable.

NO. 7 PROMOTION - In-Store Demonstration.
$35. per store
This promotion will cover a 3 day period, Thursday, Friday and Saturday. The manufacturer will supply all the necessary equipment. In-store coupon on the product to be demonstrated, may be handed out during the promotion.

ALL SUPPLIERS WILL PLEASE NOTE THE FOLLOWING:

a) Safeway requires advance notice of items to be advertised at least six weeks prior to the week of the promotion and any changes in items to be advertised must also be made six weeks in advance of promotion date.

b) All the aforementioned promotions will include a newspaper ad in the Toronto Star which is effective for all areas, for the item involved unless otherwise stated. Items do not necessarily have to appear in the regular Wednesday ad, no particular day of the ad is guaranteed. However, the advertised price will be effective for the same dates as Safeway's regular main advertisement for the week.

c) Size, type or space used to advertise paid co-operative packages will be entirely at our discretion.

d) No price reduction is guaranteed on any paid co-operative promotion.

e) Suppliers are requested to limit the number of items to be promoted to one per promotional package except for promotion number 1.

f) At the conclusion of each promotion, we will forward our charges on a debit memo. All debit memos are payable no later than thirty (30) days from the date of the invoice. All debit memos not paid within thirty (30) days will be deducted from your next purchase invoice.

g) We reserve the right to reject items which in our opinion, do not warrant advertising support.

h) We will not accept promotional offers which are not offered to the trade on a proportionately equal basis.

i) We reserve the right to advertise Safeway Brands in the same ad with like paid co-operative advertised items.

j) Flyers and handbills may be substituted for regular newspaper advertising on any week at our discretion.

k) All items will have a shelf price marker in all Safeway Toronto Zone Stores.

l) We reserve the right to revise the rates of promotional and display packages.

Yours very truly,

CANADA SAFEWAY LIMITED

APPENDIX 8

SAMPLE OF RETAILER'S PRODUCT INFORMATION SHEET AND WARRANTY

Form 11011A Rev. 3/78

THE GREAT ATLANTIC & PACIFIC COMPANY OF CANADA, LIMITED

PRODUCT PRESENTATION FORM
New Product or Off Label Deal

Please TYPE or PRINT using one form for each item.
Each presentation should have two product samples.
All presentations must comply with Federal, Provincial and Local Government Regulations

BUYER PRESENTED TO ______________________ DATE ______________________

BRAND, COMMODITY AND GRADE VENDOR ITEM CODE	SIZE	PACK	CS. WGT.	CASE SIZE IN INCHES Length ____ Width ____ Height ____ Cube

Cost per case	Terms of Payment	Prepriced Yes ____ No ____	Leak & Swell Allowance	PALLET PATTERN TI - HI -

i. Tor. Whse. ____ Mtl. Whse. ____ Dir. Dely ____________ OR f.o.b. where? ____________

Introductory Allowances ____________ From ________ To ________ How Paid ____________

Other Allowances ____________ How Paid ____________

Guaranteed Sale ____________ Floor Stock Protection Policy ____________ Bilingual Label ____________

Product Liability Insurance Yes ________ No ________

Retail Sales Tax Applicable — Ontario Yes ____ No ____; Quebec Yes ____ No ____

Co-op Funds

Volume Rebate Yes ____ No ____
Amount ____________
Include for volume only ____________

Competition now listed	Dom.	Lob.	MFM	FD CTY	OK ECON.	Loeb W.M.	Safwy				
Selling Price											

NOTE: By signing this form you are confirming that this offer is available on a like basis to all Direct Buyers.

INVOICED BY	SALES AGENT
Address	Address
Phone	Phone REPRESENTATIVE'S SIGNATURE

* *

APPENDIX 9

EXISTING AND PROPOSED LEGISLATION

Combines Investigation, R.S., c. C-23

as amended

Sections 34, 35, 2, 33

34. (1) Every one engaged in a business who

(*a*) is a party or privy to, or assists in, any sale that discriminates to his knowledge, directly or indirectly, against competitors of a purchaser of articles from him in that any discount, rebate, allowance, price concession or other advantage is granted to the purchaser over and above any discount, rebate, allowance, price concession or other advantage that, at the time the articles are sold to such purchaser, is available to such competitors in respect of a sale of articles of like quality and quantity;

(*b*) engages in a policy of selling products in any area of Canada at prices lower than those exacted by him elsewhere in Canada, having the effect or tendency of substantially lessening competition or eliminating a competitor in such part of Canada, or designed to have such effect; or

(*c*) engages in a policy of selling products at prices unreasonably low, having the effect or tendency of substantially lessening competition or eliminating a competitor, or designed to have such effect,

is guilty of an indictable offence and is liable to imprisonment for two years.

(2) It is not an offence under paragraph (1)(*a*) to be a party or privy to, or assist in any sale mentioned therein unless the discount, rebate, allowance, price concession or other advantage was granted as part of a practice of discriminating as described in that paragraph.

(3) Paragraph (1)(*a*) shall not be construed to prohibit a cooperative association, credit union, caisse populaire or cooperative credit society from returning to its members, suppliers or customers, the whole or any part of the net surplus made in its operations in proportion to the acquisition or supply of articles from or to such members, suppliers or customers. R.S., c. C-23, s. 34; 1974-75-76, c. 76, s. 16.

35. (1) In this section, "allowance" means any discount, rebate, price concession or other advantage that is or purports to be offered or granted for advertising or display purposes

and is collateral to a sale or sales of products but is not applied directly to the selling price.

(2) Every one engaged in a business who is a party or privy to the granting of an allowance to any purchaser that is not offered on proportionate terms to other purchasers in competition with the first-mentioned purchaser, (which other purchasers are in this section called "competing purchasers"), is guilty of an indictable offence and is liable to imprisonment for two years.

(3) For the purposes of this section, an allowance is offered on proportionate terms only if

(*a*) the allowance offered to a purchaser is in approximately the same proportion to the value of sales to him as the allowance offered to each competing purchaser is to the total value of sales to such competing purchaser,

(*b*) in any case where advertising or other expenditures or services are exacted in return therefor, the cost thereof required to be incurred by a purchaser is in approximately the same proportion to the value of sales to him as the cost of such advertising or other expenditures or services required to be incurred by each competing purchaser is to the total value of sales to such competing purchaser, and

(*c*) in any case where services are exacted in return therefor, the requirements thereof have regard to the kinds of services that competing purchasers at the same or different levels of distribution are ordinarily able to perform or cause to be performed. R.S., c. C-23, s. 35; 1974-75-76, c. 76, s. 17.

"merger" means the acquisition by one or more persons, whether by purchase or lease of shares or assets or otherwise, of any control over or interest in the whole or part of the business of a competitor, supplier, customer or any other person, whereby competition

(*a*) in a trade, industry or profession,

(*b*) among the sources of supply of a trade, industry or profession,

(*c*) among the outlets for sales of a trade, industry or profession, or

(*d*) otherwise than in paragraphs (*a*), (*b*) and (*c*),

is or is likely to be lessened to the detriment or against the interest of the public, whether consumers, producers or others;

"monopoly" means a situation where one or more persons either substantially or completely control throughout Canada or any area thereof the class or species of business in which they are engaged and have operated such business or are likely to operate it to the detriment or against the interest of the public, whether consumers, producers or others, but a situation shall not be deemed a monopoly within the meaning of this definition by reason only of the exercise of any right or enjoyment of any interest derived under the *Patent Act*, or any other Act of the Parliament of Canada;

33. Every person who is a party or privy to or knowingly assists in, or in the formation of, a merger or monopoly is guilty of an indictable offence and is liable to imprisonment for two years. 1960, c. 45, s. 13.

<u>Robinson-Patman Act,</u> June 19, 1936

C. 592, 49 Stat. 1526

ROBINSON-PATMAN ACT, June 19, 1936
C. 592, 49 Stat. 1526

74th CONGRESS. SESS. II. CH. 592. JUNE 19, 1936.

[CHAPTER 592]

AN ACT

June 19, 1936
[H. R. 8442]
Public, No. 692.

To amend section 2 of the Act entitled "An Act to supplement existing laws against unlawful restraints and monopolies, and for other purposes", approved October 15, 1914, as amended (U.S. C., title 15, sec. 13), and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Antitrust Act of 1914, amendment.
Vol. 38, p. 730
U.S. C., p. 510.

That section 2 of the Act entitled "An Act to supplement exisitng laws against unlawful restraints and monopolies, and for other purposes", approved October 15, 1914, as amended (U.S. C., title 15, sec. 13), is amended to read as follows:

Discriminations in price between different purchasers.

"Sec. 2.

(a) That it shall be unlawful for any person engaged in commerce, in the course of such commerce, either direct or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchases involved in such discrimina tion are in commerce, where such commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, and where the effect of such discrimina tion may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimina tion, or with customers of either of them:

Lessening, etc., competition

Provisos.
Differentials.

Quantity limits.

Provided, That nothing herein contained shall prevent differentials which make only due allowance for difference in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered:

Provided, however, That the Federal Trade Commission may, after due investigation and hearing to all interested part fix and establish quantity limits, and revise the same as it finds necessary, as to particular commodities or classes of commodities, where it finds that available purchasers in greater quantities are so few as to render differential on account thereof unjustly discriminatory or promotive of monopoly in any line of commerce; and the foregoing shall

then not be construed to permit differentials based on differences in quantities greater than those so fixed and established:

Selection of customers.

And provided further, That nothing herein contained shall prevent persons engaged in sell goods, wares, or merchandise in commerce from selecting their own customers in bona fide transactions and not in restraint of trade:

Price changes.

And provided further, That nothing herein contained shall prevent price changes from time to time where in response to changing conditions affecting the market for or the marketability of the goods concerned, such as but not limit to actual or imminent deterioration of perishable goods, absolescence of seasonal goods, distress sales under court process, or sales in good faith in discontinuance of business in the goods concerned.

Hearing on complaint.

Burden of proof.

"(b) Upon proof being made, at any hearing on a complaint under this section, that there has been discrimination in price or services or facilities furnished, the burden of rebutting the prima-facie case thus made by showing justification shall be upon the person charged with a violation of this section, and unless justification shall be affirmatively shown, the Commission is authorized to issue an order terminating the discrimination:

Proviso.

Lower price made in good faith to meet competition.

Provided, however, That nothing herein contained shall prevent a seller rebutting the prima-facie case thus made by showing that his lower price or the furnishing of services or facilities to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor, or the services or facilities furnished by a competitor.

Brokerage, etc., payments.

Payment for services rendered.

"(c) That it shall be unlawful for any person engaged in commerce, in the course of such commerce, to pay or grant, or to receive or accept, anything of value as a commission, brokerage, or other compensation, or any allowance or discount in lieu thereof, except for services rendered in connection with the sale or purchase of goods, wares, or merchandise, either to the other party to such transaction or to an agent, representative, or other intermediary is acting in fact for or in behalf, or is subject to the direct or indirect control, of any party to such transaction other than the person by whom such compensation is so granted or paid.

Discriminatory payments by seller to buyer for services, etc.

"(d) That it shall be unlawful for any person engaged in commerce to pay or contract for the payment of anything of value to or for the benefit of customer fo such person in the course of such commerce as compensation or in consideration for any services or facilities furnished by or through such customer in connection with the processing, handling, sale, or offering for sale of any products or commodities manufactured, sold, or offered for sale by such

person, unless such payment or consideration is available on proportionally equal terms to all other customers competing in the distribution of such products or commodities.

Furnishing services or facilities by seller to a buyer upon terms not accorded to all buyers.

"(e) That it shall be unlawful for any person to discriminate in favour of one purchaser against another purchaser or purchasers of a commodity bought for resale, with or without processing, by contracting to furnish or furnishing, or by contributing to the furnishing of, any services or facilities connected with the processing, handling, sale, or offering for sale of such commodity so purchased upon terms not accorded to all purchasers on proportionally equal terms.

Inducing or receiving discrimination in prices.

"(f) That it shall be unlawful for any person engaged in commerce, in the course of such commerce, knowingly to induce or receive a discrimination in price which is prohibited by this section."

Pending litigation, etc.
Vol. 38, p. 730.

Sec. 2.

That nothing herein contained shall affect rights of action arising, or litigation pending, or orders of the Federal Trade Commission issued and in effect or pending on review, based on section 2 of said Act of October 15, 1914, prior to the effective date of this amendatory Act:

Proviso.
Pending orders of Federal Trade Commission

Proceedings where violation committed.

Report of findings.

Review and enforcement of Commission's orders.
Vol. 36, p. 734, Vol. 43, p. 1103.

Provided, That where, prior to the effective date of this amendatory Act, the Federal Trade Commission has issued an order requiring any person to cease and desist from a violation of section 2 of said Act of October 15, 1914, and such order is pending on review or is in effect, either as issued or as affirmed or modified by a court of competent jurisdiction, and the Commission shall have reason to believe that such person has committed, used or carried on, since the effective date of this amendatory Act, or is committing, using or carrying on, any act, practice or method in violation of any of the provisions of said section 2 as amended by this Act, it may reopen such original proceeding and may issue and serve upon such person its complaint, supplementary to the original complaint, stating its charges in that respect. Thereupon the same proceedings shall be had upon such supplementary complaint as provided in section 11 of said Act of October 15, 1914. If upon such hearing the Commission shall be of the opinion that any act, practice, or method charged in said supplementary complaint has been committed, used, or carried on since the effective date of this amendatory Act, or is being committed, used or carried on, in violation of said section 2 as amended by this Act, it shall make a report in writing in which it shall state its findings as to the facts and shall issue and serve upon such person its order modifying or amending its original order to include any additional violations of law so found. Thereafter the provisions of section 11 of said Act of October 15, 1914, as to review and enforcement of orders

of the Commission shall in all things apply to such modified or amended order. If upon review as provided in said section 11 the court shall set aside such modified or amended order, the original order shall not be affected thereby, but it shall be and remain in force and effect as fully and to the same extent as if such supplementary proceedings has not been taken.

BILL C - 13

Sections 31.77, 34, 35

31.77 (1) Subject to subsection (2), where, on application by the Competition Policy Advocate, and after affording every person against whom an order is sought a reasonable opportunity to be heard, the Board finds that

(*a*) any supplier of an article is engaging in a practice of supplying the article to different customers who are in competition with each other at prices which differ according to the different quantities purchased by them from the supplier,

(*b*) the supplier referred to in paragraph (*a*) is a major supplier in a market or is one of the suppliers in a market where the practice is widespread, and

(*c*) the practice has impeded, or is likely to impede, substantially, the expansion of an efficient firm, or a firm that, but for the practice, would be a strong competitor in a market,

the Board may make an order directed to the supplier prohibiting him from engaging in future in the practice unless it is based on an assessment described in subsection (2).

(2) No order may be made against a supplier under this section where the Board is satisfied by that supplier that the practice described in paragraph (1)(*a*) that is engaged in by him is based on a reasonable assessment of the difference in the actual or anticipated cost of supplying customers in different quantities and under different terms and conditions of delivery.

34. (1) Every one engaged in a business who

(*a*) is a party or privy to, or assists in, any sale or offer for sale of articles that discriminates to his knowledge, directly or indirectly between any of his customers who are in competition with each other for a share of the patronage of the same ultimate customers or between any of his customers and a person acting on behalf of persons one at least of whom is in competition with such customer for a share of the patronage of the same ultimate customers,

(*b*) engages in a policy of selling products in any area of Canada at prices lower than those exacted by him elsewhere in Canada, having the effect or

tendency of substantially lessening competition or eliminating a competitor in such part of Canada, or designed to have such effect, or

(*c*) engages in a policy of selling products at prices abnormally low, having the effect or tendency of substantially lessening competition or eliminating a competitor, or designed to have such effect,

is guilty of an indictable offence and is liable to imprisonment for two years.

(2) For the purposes of this section discrimination occurs where any discount rebate, allowance, price concession or other advantage is granted or offered to one customer over and above any discount rebate, allowance, price concession or other advantage that, at the time the articles are sold or offered for sale to such customer, is available to each competing customer, or to a person acting on behalf of persons at least one of whom is a competing customer, on an offer to purchase articles of like quality in like quantity under substantially the same terms and conditions of delivery.

(3) It is not an offence under this section to be a party or privy to, or assist in any sale or offer for sale mentioned therein unless the discount, rebate, allowance, price concession or other advantage was granted as part of a practice of discrimination as described in subsection (2).

(4) This section shall not be construed to prohibit a cooperative association, credit union, caisse populaire or cooperative credit society from returning to its members, suppliers or customers the whole or any part of the net surplus made in its operations in proportion to the acquisition or supply of articles from or to such members, suppliers or customers."

35. (1) In this section, "allowance" means any discount, rebate, price concession or other advantage that is or purports to be offered or granted for advertising or display purposes and is collateral to a sale or sales of products but is not applied directly to the selling price.

(2) Every one engaged in a business who is a party or privy to the granting of an allowance to any purchaser that is not offered on proportionate terms to other purchasers in competition with the first-mentioned purchaser, (which other purchasers are in this section called "competing purchasers"), is guilty of an indictable offence and is liable to imprisonment for two years.

(3) For the purposes of this section, an allowance is offered on proportionate terms only if

(*a*) the allowance offered to a purchaser is in approximately the same proportion to the value of sales to him as the allowance offered to each competing purchaser is to the total value of sales to such competing purchaser,

(*b*) in any case where advertising or other expenditures or services are exacted in return therefor, the cost thereof required to be incurred by a purchaser is in approximately the same proportion to the value of sales to him as the cost of such advertising or other expenditures or services required to be incurred by each competing purchaser is to the total value of sales to such competing purchaser, and

(*c*) in any case where services are exacted in return therefor, the requirements thereof have regard to the kinds of services that competing purchasers at the same or different levels of distribution are ordinarily able to perform or cause to be performed. R.S., c. C-23, s. 35; 1974-75-76, c. 76, s. 17.

ONTARIO FEDERATION OF AGRICULTURE PROPOSAL

introduced in testimony before the Commission

October 24, 1979

1. THAT IT IS ILLEGAL TO DISCRIMINATE IN PRICE TO DIFFERENT PURCHASERS OF GOODS OF LIKE GRADE AND QUALITY, WHEN SUCH DISCRIMINATION MAY TEND TO CREATE A MONOPOLY OR TO SUBSTANTIALLY DECREASE COMPETITION OR TO INJURE COMPETITION WITH ANY PERSON WHO GRANTS OR KNOWINGLY RECEIVES THE BENEFIT OF SUCH DISCRIMINATION, OR WITH CUSTOMERS OF EITHER OF THEM.

   BUT (1a) THAT SUCH DISCRIMINATION IS A JUSTIFIED AND LEGAL PRICE DIFFERENTIATION WHEN IT ALLOWS FOR DIFFERENCES IN THE AVERAGE VARIABLE COSTS OF MANUFACTURE, SALE, OR DELIVERY RESULTING FROM DIFFERING METHODS OR QUANTITIES IN WHICH GOODS TO DIFFERENT PURCHASERS ARE SOLD OR DELIVERED.

   AND (1b) THAT SUCH DISCRIMINATION IS NOT UNLAWFUL WHEN IT IS MADE IN GOOD FAITH TO MEET THE LOW PRICE OF A COMPETITOR.

2. THAT IT IS UNLAWFUL FOR A CORPORATION TO PAY ANY CUSTOMER FOR SERVICE OR FACILITIES RENDERED BY THAT CUSTOMER IN RESPECT OF THE SALE OF GOODS, UNLESS SUCH A PAYMENT IS AVAILABLE ON PROPORTIONATELY EQUAL TERMS TO ALL OTHER COMPETING CUSTOMERS.

3. THAT IT IS UNLAWFUL FOR ANY FIRM TO FURNISH OR PERFORM SERVICES OR FACILITIES HAVING REGARD TO THE SALE OF GOODS UNLESS SUCH SERVICES OR FACILITIES ARE OFFERED TO ALL CUSTOMERS.

4. THAT IT IS ILLEGAL FOR A PERSON ENGAGED IN COMMERCE TO GRANT OR TO RECEIVE ANYTHING OF VALUE AS A BROKERAGE OR COMMISSION OR IN LIEU OF BROKERAGE EXCEPT FOR SERVICES ACTUALLY RENDERED IN CONNECTION WITH THE SALE OR DISTRIBUTION OF GOODS, WHETHER RENDERED TO THE BUYER OR TO AN AGENT WHO REPRESENTS OR IS CONTROLLED BY THE BUYER.

5. THAT IS IS UNLAWFUL FOR ANY PERSON ENGAGED IN COMMERCE KNOWINGLY TO INDUCE OR RECEIVE A DISCRIMINATION IN PRICE, OR TO INDUCE OR RECEIVE MORE THAN PROPORTIONAL ALLOWANCES FOR SERVICES THAN COMPETITORS, AS PROSCRIBED ABOVE IN PARAGRAPHS (1), (2), AND (3).

THE ONTARIO GOVERNMENT SHOULD AUGMENT THE POWERS AND STAFFING OF THE BUSINESS PRACTICES DIVISION OF THE MINISTRY OF CONSUMER & COMMERCIAL RELATIONS, GIVING IT AUTHORITY TO INVESTIGATE PRACTICES RELATING TO PRICE DISCRIMINATION AND TO BRING ACTIONS IN CIVIL COURT TO RECOVER DAMAGES FOR

OFFENCES AGAINST THE PRICE DISCRIMINATION PROHIBITIONS, AND TO SEEK INJUNCTIONS PROHIBITING SPECIFIC ACTIONS FOUND IN VIOLATION. IN ADDITION INJURED PARTIES WOULD HAVE AUTHORITY TO BRING SUIT TO RECOVER DAMAGES RESULTING FROM VIOLATION.

I. BAN ON DISCOUNTS TO FARMERS AND GROWER-PACKERS

OFA RECOMMENDS THAT THE ONTARIO GOVERNMENT AMEND THE FARM PRODUCTS MARKETING ACT TO MAKE ILLEGAL ALL DISCOUNTS OR OTHER REDUCTIONS IN PRICE TO FARMERS, GROWERS, AND GROWER-PACKERS.

III. VERTICAL AND HORIZONTAL INTEGRATION

THE ONTARIO GOVERNMENT ENACT LEGISLATION GIVING THE BUSINESS PRACTICES DIVISION THE POWER TO PROHIBIT AND DISALLOW PROPOSED VERTICAL AND HORIZONTAL MERGERS WHICH WILL DAMAGE COMPETITION.

IV. PRIVATE LABEL MERCHANDISE

THAT THE ONTARIO GOVERNMENT PASS LEGISLATION TO REQUIRE THAT ALL PACKAGED AND LABELLED GROCERY GOODS WHICH ARE MANUFACTURED, PACKAGED, AND LABELLED IN ONTARIO, OR WHICH ARE PURCHASED BY RETAILERS FOR SALE IN ONTARIO, SHALL CARRY PROMINENTLY ON THE LABEL THE NAME AND LOCATION OF THE MANUFACTURER OR PACKER.

V. COMPETITION FOR SHOPPING CENTRE LOCATIONS AND IN ECONOMIC DEVELOPMENT

2. CAREFULLY REVIEW THE DEVELOPMENT PLANNING PROCEDURES AS TO THE OPPORTUNITIES FOR INDEPENDENT RETAILERS TO SECURE LOCATIONS IN SHOPPING CENTRES AND OTHER KEY GROWTH COMMERCIAL AREAS, AND TAKE WHATEVER MEASURES NECESSARY TO ASSURE EQUAL COMPETITIVE OPPORTUNITIES FOR INDEPENDENT RETAIL GROCERS.

3. TAKE A DELIBERATE AND OPEN POSITION THAT THE GOVERNMENT ENCOURAGES SURVIVAL OF INDEPENDENT FOOD PROCESSORS AND DISTRIBUTORS, AND THAT IT WILL TAKE FURTHER MEASURES IF IT BECOMES CLEAR THAT THE LEGISLATION PROPOSED ABOVE IS NOT EFFECTIVE IN ANY AREA IN CURBING ECONOMIC CONCENTRATION OR IS BEING EVADED OR EFFECTIVELY ELUDED.

ONTARIO LIBERAL PARTY PROPOSAL

INTRODUCED IN TESTIMONY BEFORE THE COMMISSION

SEPTEMBER 27, 1979

1. That no one carrying on business in Ontario shall engage in the unfair marketing of farm products;

2. That for the purposes of this legislation unfair marketing practices be defined as:

(A) The requirement by a buyer other than a consumer of a farm product, as a condition of doing business, that a seller of that product grant or offer to the buyer a marketing advantage by way of discount, rebate, allowance or other price concession which is not available at the same time to other buyers of the product under substantially the same terms and conditions of sale and delivery.

(B) The granting or offering by a seller of a farm product of a marketing advantage by way of discount, rebate, allowance or other price concession to a buyer which is not made available at the same time to other buyers who offer to purchase the product under substantially the same terms and conditions of sale and delivery.

(C) The requirement by a buyer, as a condition of doing business, that a seller of a farm product grant or offer to the buyer a price concession in consideration of services provided by the buyer where the buyer knows the cost of the services provided do not approximately equal the price concession granted or offered by the seller.

3. That unfair marketing practice does not include the selling or offering to sell farm products of like quality and quantity at different prices when the seller can show the price differences were justified because of:

(1) differences in the cost of producing, processing or marketing the farm product;

(2) the need to meet price competition;

(3) the actual or imminent deterioration

4. That the Farm Products Marketing Board be empowered to conduct, on its own initiative or upon complaint, investigations of suspected unfair marketing practices and to issue cease and desist orders where such practices are found.

5. That significant fines and penalties be provided when persons or corporations are convicted in court for engaging in unfair marketing practices or for failing to comply with a cease and desist order.

APPENDIX 10

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BIBLIOGRAPHY

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